

AR 35

Annual Report

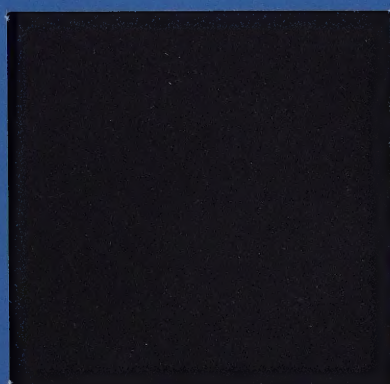
Fiscal Year Ending
June 30, 1976

The Quaker Oats Company



Since 1877





Ninety-nine years ago, on September 4, 1877, the trademark of The Quaker Man was officially registered with the U.S. Patent Office; we are now entering the 100th anniversary year.

A very early rendering of The Quaker Man is shown below.

Over the years, the trademark was modified and extended to cover a variety of wholesome food products marketed internationally as well as in the United States. Today, it is one of the best known



business symbols in the world — synonymous, as always, with high standards of quality and value.



The Quaker Man has been updated many times to keep him contemporary with trends in packaging. One particularly warm and friendly version is the current trademark for Quaker Oats and many other consumer products marketed under the Quaker name.



QUAKER

The Quaker corporate trademark, a contemporary rendition of The Quaker Man, was created in 1970 to represent the Company as a whole. This modern design continues to symbolize the traditional values for which The Quaker Man was first chosen a hundred years ago.

Other well known Company brands and trademarks are featured in a special section beginning on page 52.

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The Quaker Oats Company Today

A diversified corporation that manufactures and markets worldwide a broad line of consumer products and specialty chemicals.

The Grocery Products Area includes: in the U.S. and Canada — hot and ready-to-eat cereals; mixes, syrup, and corn products; frozen foods and pet foods. Internationally — cereals, pet foods, mixes, nutritional beverages, chocolate products, and canned seafood.

The Diversified Businesses Area includes: preschool and school-age toys, art and craft kits and mail order, specialty chemicals, crepe restaurants, and specialty cookies and crackers.

Automatic Dividend Reinvestment

This voluntary service, offered by the Company since 1971, provides a simple and inexpensive way for owners of Quaker common stock to use their dividends to purchase additional shares on a continuing basis. Cash investments may also be made. For further information, please write or call the Secretary's Office.

Annual Meeting

All shareholders are encouraged to attend the annual meeting, which will be held this year on Wednesday, November 10, 1976, in the sixth floor assembly room at The Northern Trust Company, 50 South LaSalle Street, Chicago, Illinois. The meeting will begin promptly at 9:30 a.m. A formal notice of this meeting and all proxy materials will be mailed to shareholders early in October. At the same time, proxies will be solicited by management.

Financial Highlights

Thousands of Dollars			
Year Ended June 30	1976	1975	Percent Increase (Decrease)
Net sales	\$1,473,052	\$1,389,013	6.1
Operating income	124,312	93,734	32.6
Interest expense (net)	13,426	26,441	(49.2)
Income before income taxes	110,886	67,293	64.8
Net income	53,093	31,037	71.1
Preferred and preference dividends	5,206	1,103	372.0
Net income available for common	47,887	29,934	60.0
Per Share			
Net income per common share	\$2.31	\$1.45	59.3
Preferred dividends declared	3.00	3.00	—
Preference dividends declared	9.56	1.35	608.2
Common dividends declared	.84	.80	5.0
Common Stock			
Average shares outstanding	20,711,092	20,699,008	0.1

Shareholder Services

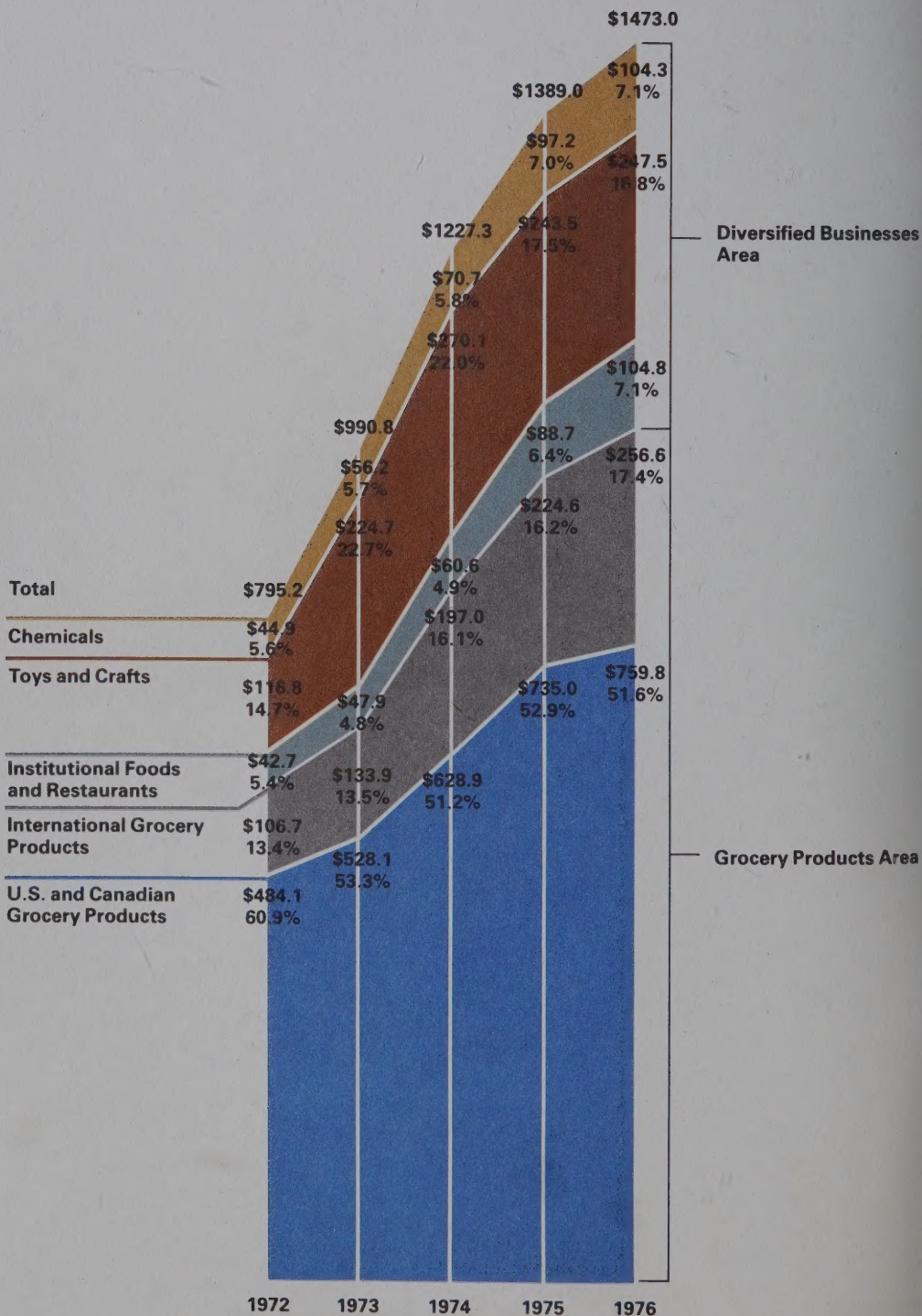
As a shareholder, please feel free to contact the Office of the Secretary about any matter related to your Quaker common, preferred or preference stock. Please write: Shareholder Services, The Quaker Oats Company, Merchandise Mart Plaza, Chicago, Illinois 60654, or telephone: (312) 222-6751.

General questions or comments about the business are always welcomed by the senior officers, who may be contacted at the same address.

Should you desire advice on any matter related to the purchase or sale of Quaker stock, please contact a stockbroker, banker or other investment advisor in your community.

Consolidated Sales

Sales in Millions of Dollars



To Our Shareholders and Employees:

Fiscal 1976 was an excellent year.

From the point of view of U.S. consumers, there was good news, as inflation rates declined, employment increased, and economic growth returned.

Internationally, economic conditions also generally improved.

In the United States, there was a revival of the national spirit and sense of purpose in celebration of the Bicentennial. We were impressed by the extent to which people around the world, including our employees, joined in recognition of the U.S. achievement.

Fiscal 1976 Earnings

There was also excellent news at Quaker. Our earnings rebounded substantially in fiscal 1976 to record levels. These record earnings were achieved despite the absorption of both substantial operating losses and a write-off in connection with the sale of the Marx Toys Division.

Earnings of \$2.31 per share are *after* the 57 cents write-off for the April sale of Marx.

The per-share earnings were 13 percent ahead of fiscal 1973, our previous record year, and 59 percent ahead of fiscal 1975.

Operations Progress

Excellent operating results were highlighted by the sharply improved profit in grocery products worldwide, and were achieved by a combination of effective management, favorable commodity costs, and a generally improved economy. All major areas of our business except the Chemicals Division had strong years. Improvements in the large grocery divisions and subsidiaries were accompanied by fine years at the Fisher-Price, Magic Pan, Burry and Needlecraft Divisions.

The Chemicals Division experienced volume softness during the year, but we continue to be optimistic about long-term potential.

Our toy business, a problem a year ago, is now in good shape. First, Fisher-Price — always inherently strong as the quality leader in its product lines — had a good year, with fine increases in sales and earnings. Prospects for Fisher-Price this coming Christmas are good. Second, we eliminated a costly problem business — Marx Toys. The sale involved substantially all of the assets of the U.S. and Canadian Marx businesses, plus the stock in Marx Hong Kong operations. We retained the successful Marx business in Mexico. (Complete details of the sale are on page 27.)

Financial Progress

We are also pleased that our better earnings were accompanied by a stronger balance sheet and improved financial ratios. In fact, our target objectives for these ratios were exceeded. New reporting systems were instituted with greater emphasis on return on invested capital. At year-end, accompanying the higher net earnings:

1. Our balance sheet is very strong.
2. Return on common shareholders' equity improved to 12.8 percent from 8.7 percent in fiscal 1975.
3. Our operating income margin, unacceptably low last year, is now at a more satisfactory level.

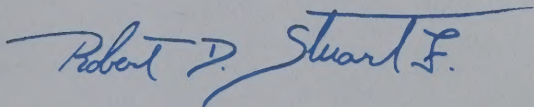
Outlook

In our Annual Report a year ago, I expressed confidence that tough, corrective measures, improved organization and more effective internal controls had strengthened our Company. Now, a year later, that observation has been confirmed by excellent performance.

More than anything else, the people of our Company produced the fine fiscal 1976 results. This Annual Report has a unique section on our employees as shareholders, beginning on page 18, and I draw your particular attention to it.

In the United States, we've been renewed by the goodwill that resulted from our nation's Bicentennial celebration, and throughout most of the world the outlook for the year ahead is encouraging. At Quaker, we're now entering the 100th anniversary year of the registration of our original Quaker Man trademark. We try constantly to keep in mind that this mark and its more contemporary versions stand for certain basic values in products, services, employment and corporate citizenship that shareholders and employees can be proud of.

In this, the 100th year of The Quaker Man, we believe we are well positioned with proven management talent, strong basic businesses, excellent financial condition and good forward momentum to meet aggressive objectives in the future.

A handwritten signature in blue ink that reads "Robert D. Stuart, Jr." The signature is fluid and cursive, with a long horizontal line extending from the end of the name.

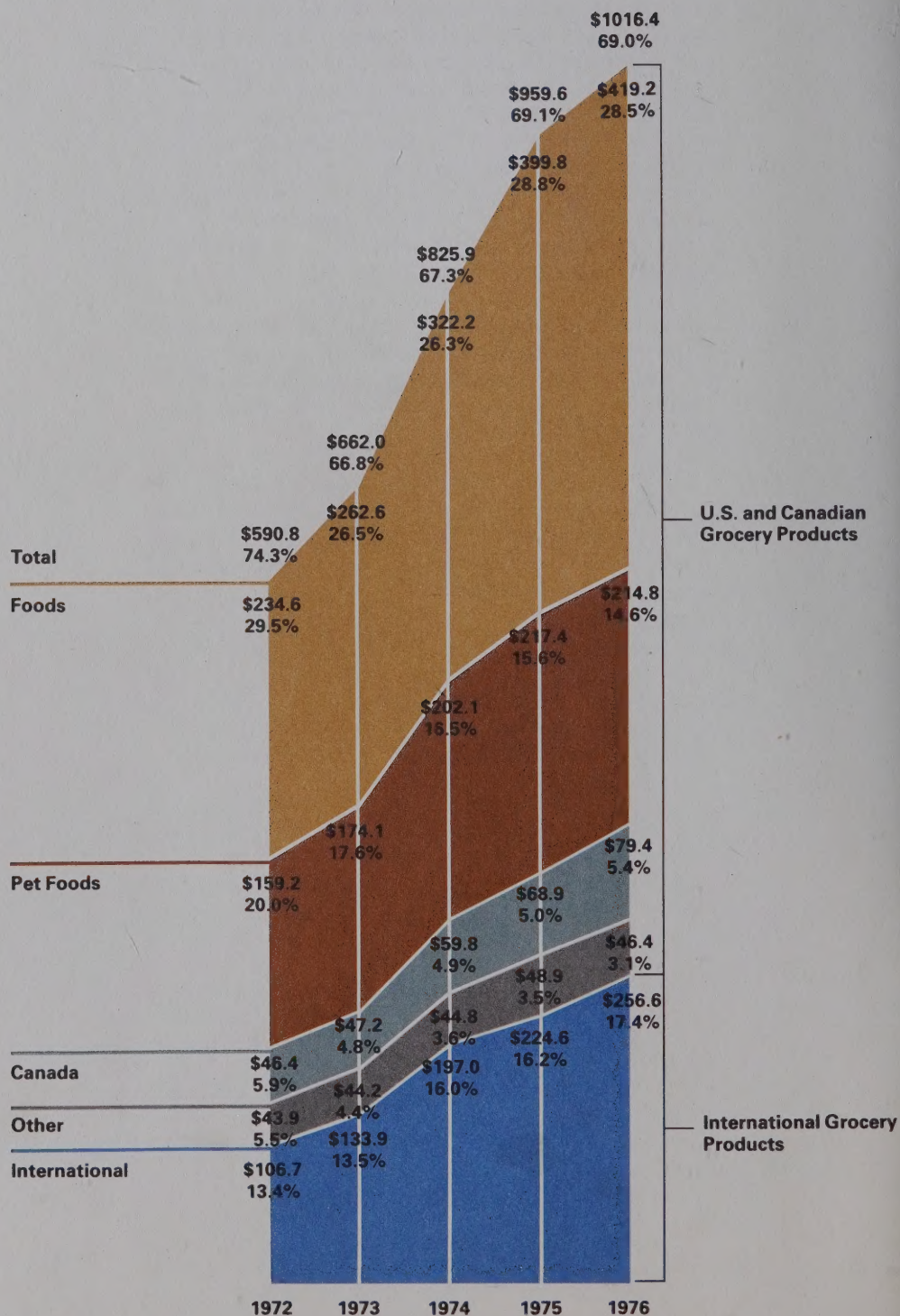
Robert D. Stuart, Jr.
President and
Chief Executive Officer

September 4, 1976

Grocery Products Area

Sales in Millions of Dollars

Percents of Consolidated Sales



Grocery Products Area

Quaker's foods and pet foods purchased by consumers in grocery stores worldwide are included in the Grocery Products Area, which accounted for 69 percent of the Company's sales in fiscal 1976. These grocery products carry some of the best-known brand names and represent some of the best values in the world.

Approximately 67 percent of the Area sales volume is in the United States, 8 percent in Canada, 14 percent in Europe, and 11 percent in Latin America and the Pacific region.

Fiscal 1976 was a very strong profit year for the Grocery Products Area. After two flat years, profits turned up substantially, and margins are now at satisfactory levels.

There were several significant elements underlying the sharp improvement in the past fiscal year:

1. More effective purchasing management and lower commodity costs were the largest factors in improved profits this year, although commodity costs remained well above levels of 1973 and earlier.
2. Margins were up significantly, despite continuing cost pressures in every area except commodities.
3. Emphasis on productivity improvements and cost controls favorably affected operating income.
4. Market shares were generally firm, supported by a 20 percent increase in marketing expenditures.
5. International sales volume and profitability were both up significantly.
6. Key management changes instituted in January, 1975, contributed significantly to the improvement. The Area organization that produced the excellent fiscal 1976 results is shown on page 50.

U.S. Foods Division

This Division is responsible for U.S. manufacturing and marketing of hot and ready-to-eat cereals, pancake mixes and syrup, corn products and frozen foods. Sales were up 5 percent. Operating income was up very substantially compared with the prior year. Marketing expenses were also up significantly from last year.

Foods Sales (Millions of Dollars)

1976	\$88.2	\$122.9	\$136.2	\$60.9	\$419.2
1975	\$94.9	\$116.1	\$134.3	\$54.5	\$399.8
1974	\$69.4	\$102.6	\$100.5	\$49.7	\$322.2
1973	\$62.9	\$77.6	\$81.5	\$40.6	\$262.6
1972	\$64.8	\$60.3	\$78.0	\$31.5	\$234.6
	Hot Cereals	Ready-to-Eat Cereals	Mixes, Pancake & Syrup	Frozen Foods	Totals

Hot Cereals Sales of both traditional and instant varieties of Quaker Oatmeal were 5 percent better than last year. The hot cereal category is a solid business, and is particularly strong when consumers are sensitive to the value of their food purchases.

Ready-to-Eat Cereals enjoyed the best profit year in the Company's history. Life cereal continued its excellent growth. This nutritional cereal has one of the best growth records in the ready-to-eat category, which as a whole is growing about 7 percent a year. Cap'n Crunch remained in a leadership position in children's cereals, even though the introduction of Punch Crunch, a fruit-flavored line extension, was not successful. In fiscal 1976 Quaker 100% Natural Cereal held its share consistently in the natural cereal market, and is now ranked as one of the top ready-to-eat cereals in the United States.

Mixes, Syrup and Corn Products Total sales of Quaker and Aunt Jemima pancake mix, cornmeal, grits, and Aunt Jemima syrup were slightly ahead of last year. This section of our business experienced increased volume during the U.S. recession. With the economic recovery, volume has stabilized, but at a higher base. Aunt Jemima continues to be the brand leader in mixes, cornmeal, and grits, and moved up to second place in the table syrup business. A new Quaker Oatmeal Cookie mix was just introduced nationally.

Frozen Food sales increased significantly during fiscal 1976. A key factor was higher sales of Celeste Frozen Pizza. Celeste now enjoys national distribution with a broad line of pizzas. The brand has a strong share of the total frozen pizza market, which is growing at well over 10 percent a year. New 10- and 8-inch sizes have been very successful additions to our line. Although our frozen waffle and French toast business has not yet recovered from recession-induced declines, this was more than made up for by strong sales of a new Aunt Jemima Frozen Pancake Batter, introduced last fall and now the leader in this specialty category. A key objective of our frozen foods business is to achieve an adequate return on investment.

Operations Significant progress was made in cereals and mixes operations during the year. Productivity was increased considerably, and cost-saving projects contributed effectively to profitability. Purchasing decision-making was reorganized at the division management level, with encouraging results.

The Foods Division operates six U.S. plants, all of which are excellent, contemporary food processing operations. Our frozen production is now concentrated at the Jackson, Tennessee, plant, one of the finest frozen food plants in the world.

S. Pet Foods Division

The Pet Foods Division achieved its fiscal 1976 objective of significantly improving profitability.

Profits were up sharply from last year's depressed levels. Both volume and dollar sales of Ken-L Ration dog food and Puss 'n Boots cat food in the U.S. were about the same as last year, in line with expectations.

Commodity costs were down. Strong management emphasis on plant productivity, product and distribution efficiencies and overhead-reduction programs contributed significantly to the profit improvement. Two small coastal plants were closed during the year, reducing overhead. The Division now operates three modern plant facilities.

Pet Food Sales (Millions of Dollars)

1976	\$38.9	\$175.9	\$214.8
1975	\$39.9	\$177.5	\$217.4
1974	\$38.6	\$163.5	\$202.1
1973	\$34.9	\$139.2	\$174.1
1972	\$36.6	\$122.6	\$159.2
	Cat Food	Dog Food	Totals

Canned dog food volume was about the same as last year, halting a downward trend. A new beef-flavored canned dog food is now in test market. Two new Ken-L Ration Burger products have performed very well — Burger 'n Egg, introduced nationally at the beginning of fiscal 1976, and Burger and Liver, introduced nationally in January. A distinctive product to compete in the dry dog food category, Ken-L Ration Tender Chunks, has just entered test market.

In cat food, the basic Puss 'n Boots canned product showed some added volume strength during the fiscal year. A new flavor, Fisherman's Platter, was successfully introduced. Puss 'n Boots Moist Meals continues to rank second in the semi-moist cat food category in the 50 percent of the U.S. market where it is sold.

Other U.S. Sales

The most distinctive business in the "Other U.S. Sales" category is our very successful Wolf Brand regional canned chili business, which operates in the southwestern United States. Sales and earnings were at record levels. Also included in this category are industrial cereal sales and sales of miscellaneous grains and by-products.

Other U.S. Sales (Millions of Dollars)

1976	\$46.4
1975	\$48.9
1974	\$44.8
1973	\$44.2
1972	\$43.9

Canada

The Quaker Oats Company of Canada Limited had a very good year, with sales up significantly and an earnings increase more than twice the rate of the sales improvement. Lower commodity costs were important, although significant production efficiencies also contributed. Prior-year business had been affected by a two-month strike at our pet food plant in Ontario.

Canadian Grocery Products Sales (Millions of Dollars)



Sales volume is about evenly divided between foods and pet foods. The Canadian Company, which recently celebrated its 75th anniversary, is a major food processor there. It is the Canadian market leader in hot cereals, pancake mix, frozen waffles and pet foods. In addition, our Quaker Harvest Crunch, similar to Quaker 100% Natural Cereal in the U.S., is the leading brand in its category.

International Grocery Products

International Grocery Products is responsible for Quaker's grocery business — about 60 percent foods and 40 percent pet foods — outside the U.S. and Canada. In terms of sales, the largest businesses are in the United Kingdom, Mexico, the Benelux countries, France, Scandinavia, Brazil and Australia, with smaller businesses in many other countries.

International sales in dollars were up 14 percent from last year, largely due to sales of Quaker France, which were included for the first time. Sales in dollars were adversely affected by foreign exchange rates. There was generally good volume growth, and operating income improved 54 percent.

International Grocery Products Sales (Millions of Dollars)



Price controls continue to be a factor in most countries where we operate. In the majority of cases, a pass-through of most cost increases is allowed, although there frequently is a lag between the dates we pay the higher costs and the later dates when they are reflected in pricing.

Europe Sales were \$141 million, with the addition of Quaker France more than accounting for the 14 percent gain over last year. In September we acquired 100% ownership of this subsidiary, which was formerly a joint venture. Profitability was up in the United Kingdom, although sales were off. Both sales and earnings improved on the Continent — particularly in pet foods.

While we have been in the cereals and mixes businesses in Europe for many years, the principal growth effort recently has been in pet foods — where overall market growth rates have been strong.

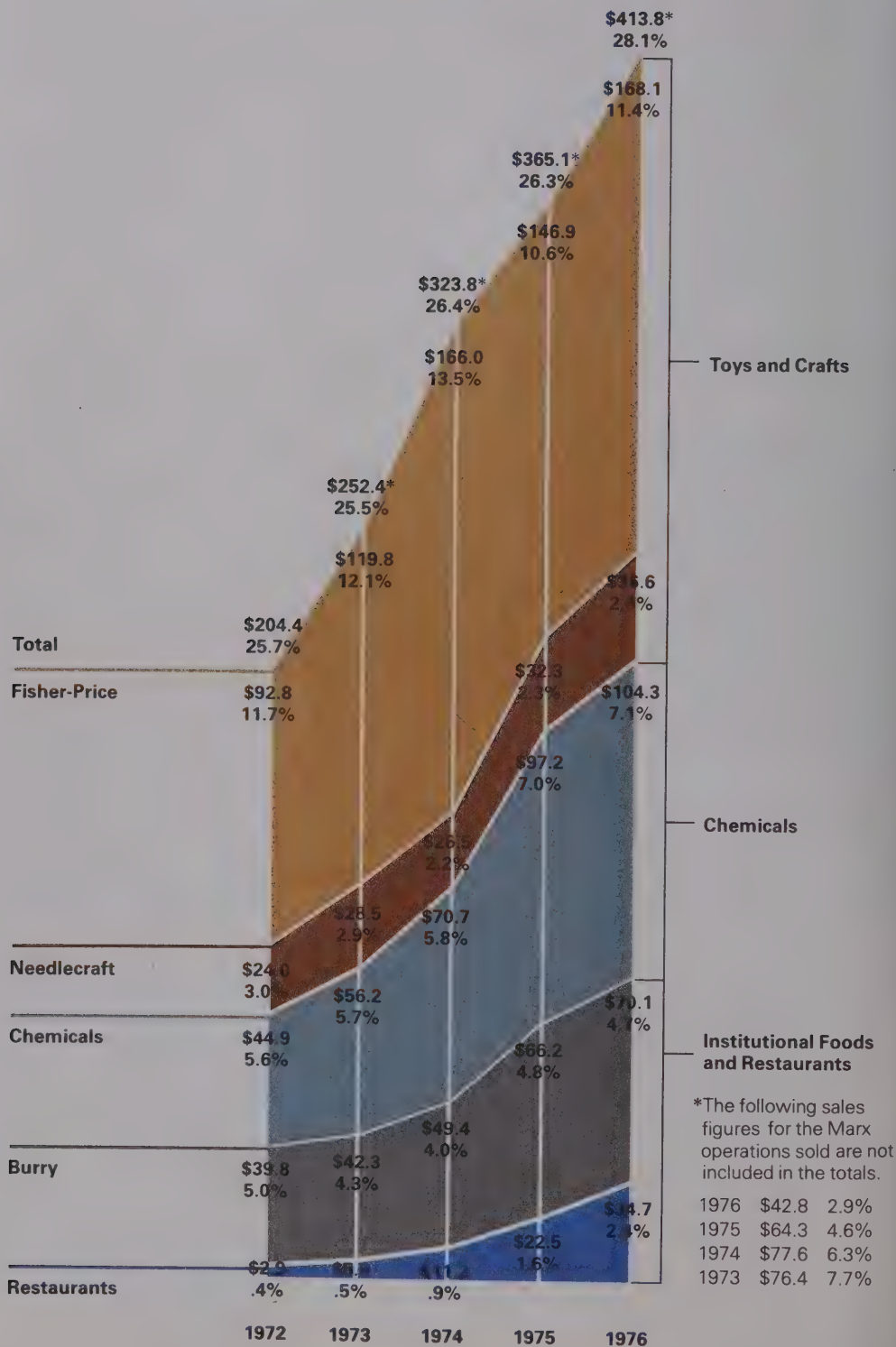
Latin America and the Pacific Sales in this region increased 15 percent from last year, to \$115 million. In Brazil there was a good volume increase in Coqueiro canned fish, as well as substantial increases in oats and corn products. There was significant turnaround from unsatisfactory sales and profit trends of the prior year in Australia, where pet foods are the focus of our business.

In Mexico, our La Azteca chocolate bar and beverage business significantly increased sales during the year. In Venezuela, volume and profitability were off. Other Latin American businesses did well.

Diversified Businesses Area

Sales in Millions of Dollars

Percents of Consolidated Sales



Diversified Businesses Area

The Diversified Businesses Area consists of five operating divisions. A common denominator among the five is that each participates in specialty markets that have attractive growth potential, including quality toys, chemicals, certain areas of the food service business, theme restaurants, art needlecraft kits and mail order crafts. Each division is headed by a President, as listed on page 51, reporting to the Executive Vice President — Diversified Businesses.

Fiscal year sales of \$413.8 million for the five continuing divisions — Fisher-Price, Chemicals, Burry, Magic Pan and Needlecraft — were up 13 percent over last year, and operating income of \$53.1 million improved 18 percent. Marx Toys, which was formerly a sixth division in this area, operated at a substantial loss. A complete discussion of the Marx sale is on page 27.

Fisher-Price Toys Division

Fiscal 1976 sales of \$168 million were up 14 percent, and operating income was very substantially above the year-ago level. This improvement in performance exceeded the objectives set for Fisher-Price for the year.

Fisher-Price Sales (Millions of Dollars)



The improving economy, coupled with better sales forecasting and tighter production and inventory controls, contributed to these results, following the recession that affected most of the toy industry in the fall of 1974.

Fisher-Price toys enjoy a well-established reputation for unique design, high-quality manufacture, and superior play value. The Fisher-Price product line includes many toys that remain in heavy demand from year to year, some of them “classics,” which form a solid basic business.

Within this framework, Fisher-Price has been broadening the scope of its product line in recent years. Starting with the extremely successful base of toys for preschool children, on which the division built its reputation, the line was extended downward in age-range to include Fisher-Price-quality products for infants. More recently, the product age-range was also moved upward to include toys for children in the early school years.

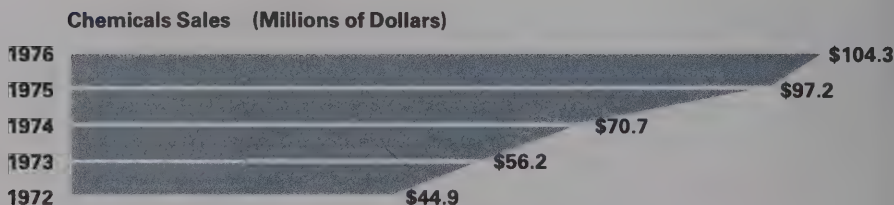
International expansion has become an important growth thrust in the division's business. Fisher-Price's superior product development capability is being applied internationally, where the division's quality manufacturing is gaining a consumer reputation. About a quarter of Fisher-Price sales are now outside the U.S., where we are incurring heavy initial marketing expenditures.

Quaker's 56 percent interest in the Marx Toys subsidiary in Mexico, Plastimarx, was retained after the sale of the other Marx operations, and is now operating as a part of Fisher-Price, with the able Mexican management continuing to run the business.

Orders, consumer interest and customer inventory levels of Fisher-Price toys are encouraging as we approach the 1976 Christmas season.

Chemicals Division

The Chemicals Division is one of the Company's significant growth opportunities over the long term. In fiscal 1976, however, the Division faced a number of problems that produced a disappointing decline in unit volume and operating income, although dollar sales were up.



Product development in this division is based on the Company's pioneering research in furan chemistry, going back more than half a century. The most important of these products is furfuryl alcohol (FA), which is widely used because it enhances the properties of resins used to bond sand for foundry cores and molds. Generally FA resins are most widely used in foundries that specialize in large-size castings. Furfural and other derivative products are used in a number of other industrial products and processes, particularly in the oil-refining, synthetic rubber and plastics industries.

Recognizing expanding markets for the division's products worldwide, the Company has made very substantial investments in recent years for large, capital-intensive production facilities in the United States and Europe. Future market development programs have also been under way in these areas and in Japan, where in fiscal 1975 a joint-venture — Kao-Quaker — was formed with the Kao Soap Company, a Japanese manufacturer of chemicals and detergents.

Because the supply of our chemicals had been insufficient to meet demand, they were on allocation for a little over two years. With increasing supplies, we were able to remove allocations in January, 1976.

At that time many customers reduced their purchases in order to work off inventories built up during the allocation period, and our largest single end user, the foundry industry worldwide, experienced a business decline. This industry historically lags behind consumer goods in both economic recession and recovery. Low pricing of competitive chemicals was also a significant factor in the market.

In fiscal 1976, these factors — combined with higher raw material costs and planned start-up expenses throughout the year for the major new furfural and furfuryl alcohol plant at Bayport, Texas, near Houston — adversely affected Chemicals Division operating results. Construction of the Texas plant was started in 1974, with full production capacity anticipated in about two years.

Division operating income during the year was reduced by a pre-tax charge of \$1.3 million related to the adoption of the LIFO method of pricing domestic Chemicals Division inventories. Unfavorable exchange rates also affected earnings, since a significant portion of the division's business is done in Europe.

Thus, a combination of factors caused operating income to be off 47 percent from the record high achieved a year ago. We cannot be certain when a significant upward trend will resume. We do, however, remain confident that this business has fine potential.

Burry Division

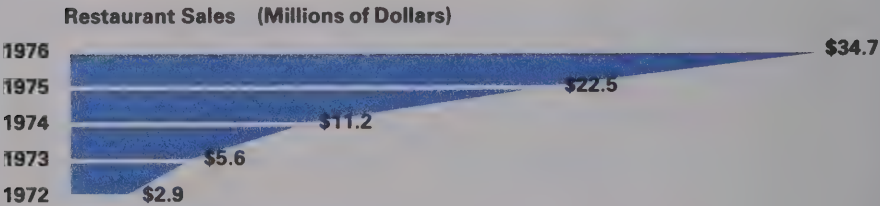
Burry products include specialty bakery products for four different markets — cookies for sale by Girl Scouts, wafers for ice-cream sandwich producers, institutional products made by both Quaker and Burry for the food service trade, and, in the Eastern section of the United States, cookies and crackers sold in grocery stores.



Division sales increased 6 percent from last year. Profits were at record levels for the second consecutive year.

**Magic Pan
Division**

Magic Pan opened 10 new locations in fiscal 1976, bringing the total of these specialty restaurants to 38. Sales were up 54 percent, and earnings more than doubled. While the new restaurants added to overall sales, performance of the 28 restaurants that were opened prior to fiscal 1976 continued to grow. Significant additional potential is projected both in new locations and in the steadily expanding volume of existing units.



Menus feature outstanding crepes, palacsintas and other distinctive entrees for luncheon, dinner and late-evening dining served in an attractive, relaxing atmosphere. New menu items created by the Magic Pan staff are added selectively, all in the context of a basic concept that has made these restaurants so successful.

Twenty new restaurants are expected to be opened during fiscal 1977. We opened our first restaurant outside the U.S. during the year in Toronto, and expect to open three more in Canada this year.

**Needlecraft
Division**

Sales and operating income of the Needlecraft Division increased significantly in fiscal 1976.



The Needlecraft Division markets a wide range of needlework products sold through retail outlets, and operates Herrschners, Inc., a mail-order business. Both our needlecraft kits and the specialty mail order business have promising growth potential.

An attractive line of Wonder Art latchhook rug kits and supplies was introduced during the year. Plant expansions at LaFayette, Georgia, and Stevens Point, Wisconsin, were completed, and more recently a small plant at Fort Atkinson, Wisconsin, was closed to consolidate production.

Quaker's People Are Shareholders Too

The Quaker Man, whose hundredth year we are observing, represents a century-old tradition of wholesome quality products. He also represents people—thousands of them, who care about this Company.

The excellent year we had in fiscal 1976 would not have happened without the efforts of everyone in our Quaker family. Almost twenty-four thousand employees worldwide, individually and as a team, made our sales and earnings reach new record levels.

Year in and year out, in record-breaking years and those that aren't, Quaker employees demonstrate their commitment to excellence in everything they do. The men and women of Quaker have a long tradition of dedication to their communities, to the betterment of their professions and trades, to public service. When "corporate social responsibility" became a focus of attention in the 1960's, it was already a well established and integral part of the Quaker philosophy, and the attitudes of our people. The same is true of "corporate ethics," where the high standards of Quaker and its people have existed for generations.

Some employees, like those pictured on the following pages, also have a commitment to Quaker's financial future beyond the value of their paychecks and employee benefits. These employees are owners of Quaker common stock, which they purchased voluntarily because they believe Quaker is a good financial investment for them as well as a good place to work.

The Company believes that employee stock ownership is beneficial to all the shareholders because it clearly unifies the interests of shareholders and employees. To create widespread employee stock ownership, to recognize the economic achievements of 200 years of the United States as a nation and a hundred years of The Quaker Man as a part of our economic system, and to salute loyal employees for their fine results

in fiscal 1976, the Board of Directors in July approved a unique employee stock award program, a portion of which is subject to shareholder approval. Under this program, a very large number of our U.S. employees will become direct share owners. We believe this will be a uniquely beneficial milestone in shareholder-employee relations.

As we add new employee shareholders, we wish to salute representative Quakers who have invested much of their time and some of their money in The Quaker Oats Company—people such as:

Alfred Nold, a packaging foreman at the St. Joseph, Missouri, cereals and mixes plant. "This Company has been good to my family and me for 35 years," he says. "I'm proud to own a small part of it."

Helen Fries, administrative aide at the Fisher-Price Toys plant in Holland, New York, says, "When I saved a few extra dollars, I wanted to purchase Quaker stock. I believe in Fisher-Price and Quaker; they're both going to be around a long, long time."

And George Weeks, area maintenance supervisor at the Cedar Rapids, Iowa, cereals, mixes and chemicals complex, adds, "Owning Quaker stock gives me the incentive to do an even better job. Now I have more reason than ever to contribute to Quaker's success."

These employees and others you'll meet in these pages are just a few of the many people who have a double investment in our Company, as both employees and shareholders. It is their commitment and their concern, we're sure, that will keep The Quaker Man smiling as he moves toward his next hundred years.

Administrative aide Helen Fries has been at the Fisher-Price plant in Holland, New York, for 15 years. With an ever-present twinkle in her eye, Helen claims to have trained many a plant manager over the years! She loves to travel, especially to visit her four young grandchildren. And she notes with some delight that "my grandchildren are being raised on Fisher-Price toys."



Dante Boschetti (right), a 25-year employee at the Burry Division plant in Elizabeth, New Jersey, is a general company driver, hauling everything from mail to butter and eggs. He looks forward to retiring in a few years to his mobile home in Florida.



Alfred Nold's 35-year involvement with Quaker is a family affair. A package foreman at the cereals and mixes plant in St. Joseph, Missouri, Al met his wife at Quaker. Sons Gregory (shown here), a microbiologist, and Michael, a bulk package foreman, are both employees at St. Joseph. And before young grandson Mark was born, daughter-in-law Jane was also a Quaker employee.

Mario Orosa (left) has been a process engineer at our John Stuart Research Laboratories in Barrington, Illinois, since 1971. Developing new and improved manufacturing and processing equipment is part of his responsibility. After hours, Mario can be found with tennis racket or camera in hand.



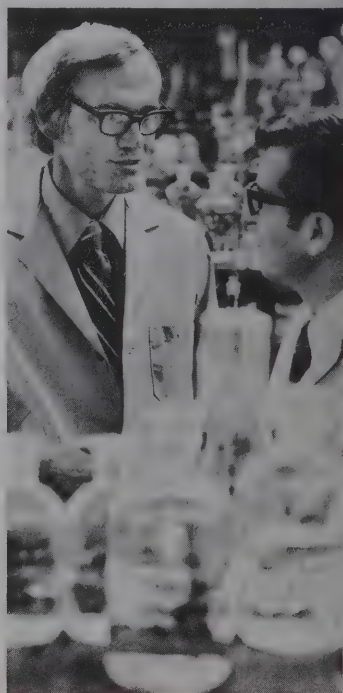
Jerry Hoffman (left), mechanic at the Shiremanstown, Pennsylvania, cereals and mixes plant, began his Quaker career at the Akron, Ohio, plant in 1948. A member of the plant's volunteer fire brigade, Jerry is also an active member of the "old timers" group there. Away from Quaker, Jerry devotes time to gardening and photography.



Kathy Loseke (left), traffic supervisor at the Omaha, Nebraska, chemicals plant, has been with the company for 23 years. She and her husband Ken have been Quaker shareholders for nearly 20 of those years. Recently named the first woman director of Delta Nu Alpha, national educational transportation organization, Kathy devotes considerable energies to new and better traffic and transportation systems.



In Ray Miller's ten years with Quaker, he's already worked at three locations, but his company affiliation is far older than that. Now manager—industrial relations, Grocery Products, at corporate headquarters in Chicago, Ray (second from left), is a fourth generation Quaker. His great-grandfather founded the Miller "dynasty" when his small mill in Akron, Ohio, became part of the American Cereal Company, forerunner of Quaker.





Area maintenance supervisor George Weeks has been at Quaker's Cedar Rapids, Iowa, cereals and mixes plant for 14 years. George devotes much of his free time to his hobby—building handcrafted guitars. Now at work on his third guitar, George spends about a year on each one. He plays the finished product too, but “only my wife Anita is allowed to listen.”

When not working as a supervising chemist at our John Stuart Research Laboratories in Barrington, Illinois, Jack Thorson (left) skis on snow and water. Jack's terrain at Quaker is the analytical laboratory, where quality control is the goal. Product formulations are continually tested here to verify label claims and other supportive data.

Ten Year Financial Summary

Millions of Dollars
Except Per Share

Year Ended June 30 ^(B)	1976	1975	1974
Net sales	\$1,473.0	\$1,389.0	\$1,227.3
Cost of goods sold	1,016.2	1,029.4	914.9
Gross profit	456.8	359.6	312.4
Selling, general and administrative expenses	304.0	256.8	215.3
Interest expense—net	13.4	26.4	21.1
Other expense (income)	28.5	9.1	(.5)
Income before income taxes and extraordinary item	110.9	67.3	76.5
Provision for income taxes	57.8	36.3	36.6
Income before extraordinary item	53.1	31.0	39.9
Extraordinary (charge) credit	—	—	—
Net income	53.1	31.0	39.9
Preferred and preference dividends	5.2	1.1	.4
Net income available for common	\$ 47.9	\$ 29.9	\$ 39.5
Per common share: (A)			
Income before extraordinary item	\$ 2.31	\$ 1.45	\$ 1.91
Extraordinary (charge) credit	—	—	—
Net income	\$ 2.31	\$ 1.45	\$ 1.91
Dividends declared	\$.84	\$.80	\$.76
Current assets	424.8	357.7	406.3
Current liabilities	209.3	149.0	221.8
Net working capital	215.5	208.7	184.5
Net fixed assets	373.6	358.2	319.3
Long-term debt	148.7	158.3	171.4
Shareholders' equity	431.8	400.7	338.4
Return on common shareholders' equity	12.8%	8.7%	11.9%

(A) Adjusted for stock splits.

(B) Results for 1972 through 1968 have been restated to reflect the July, 1972 merger with Needlecraft Corporation of America Inc., recorded as a pooling of interests. Prior years have not been restated since the effect is not material.

(C) Excludes extraordinary items.

1973	1972	1971	1970	1969	1968	1967
\$990.8	\$795.2	\$701.9	\$612.8	\$562.3	\$554.2	\$555.1
<u>692.7</u>	<u>545.8</u>	<u>482.3</u>	<u>411.8</u>	<u>382.1</u>	<u>387.9</u>	<u>403.0</u>
298.1	249.4	219.6	201.0	180.2	166.3	152.1
201.5	172.4	153.1	142.6	130.3	122.8	114.4
11.0	6.6	5.6	2.0	(.9)	.8	1.1
<u>.1</u>	<u>(.2)</u>	<u>.1</u>	<u>(.2)</u>	<u>.3</u>	<u>.6</u>	<u>.4</u>
85.5	70.6	60.8	56.6	50.5	42.1	36.2
<u>43.4</u>	<u>35.0</u>	<u>29.7</u>	<u>27.9</u>	<u>24.5</u>	<u>20.6</u>	<u>17.4</u>
42.1	35.6	31.1	28.7	26.0	21.5	18.8
<u>—</u>	<u>—</u>	<u>(5.9)</u>	<u>—</u>	<u>(1.1)</u>	<u>—</u>	<u>.9</u>
42.1	35.6	25.2	28.7	24.9	21.5	19.7
.4	.5	.5	.5	.5	.5	.5
<u>\$ 41.7</u>	<u>\$ 35.1</u>	<u>\$ 24.7</u>	<u>\$ 28.2</u>	<u>\$ 24.4</u>	<u>\$ 21.0</u>	<u>\$ 19.2</u>
\$ 2.04	\$ 1.78	\$ 1.56	\$ 1.45	\$ 1.33	\$ 1.11	\$.97
<u>—</u>	<u>—</u>	<u>(.30)</u>	<u>—</u>	<u>(.06)</u>	<u>—</u>	<u>.05</u>
<u>\$ 2.04</u>	<u>\$ 1.78</u>	<u>\$ 1.26</u>	<u>\$ 1.45</u>	<u>\$ 1.27</u>	<u>\$ 1.11</u>	<u>\$ 1.02</u>
<u>\$.72</u>	<u>\$.68</u>	<u>\$.67</u>	<u>\$.63</u>	<u>\$.58</u>	<u>\$.53</u>	<u>\$.49</u>
313.8	247.7	199.9	185.8	149.7	149.3	137.4
<u>157.7</u>	<u>116.7</u>	<u>89.3</u>	<u>94.3</u>	<u>68.5</u>	<u>65.3</u>	<u>57.9</u>
156.1	131.0	110.6	91.5	81.2	84.0	79.5
272.1	243.9	200.4	181.3	142.6	129.1	116.2
<u>123.8</u>	<u>131.5</u>	<u>96.4</u>	<u>68.8</u>	<u>18.9</u>	<u>21.4</u>	<u>22.9</u>
312.8	259.6	232.0	217.7	197.2	184.6	169.2
13.6%	14.0%	13.7% (C)	13.4%	13.5% (C)	11.7%	11.1% (C)

Financial Review

Sales in fiscal 1976 were \$1.473 billion, compared with \$1.389 billion in the prior year and \$1.227 billion in fiscal 1974.

Unit volume was relatively stable on an overall basis in fiscal 1976. Two factors in the 6 percent sales increase were the full-year impact of price increases instituted during the prior year, and the addition for the first time of sales of Quaker France, a wholly owned subsidiary that previously was a joint venture. The 13 percent sales increase in fiscal 1975 over fiscal 1974 largely resulted from price increases.

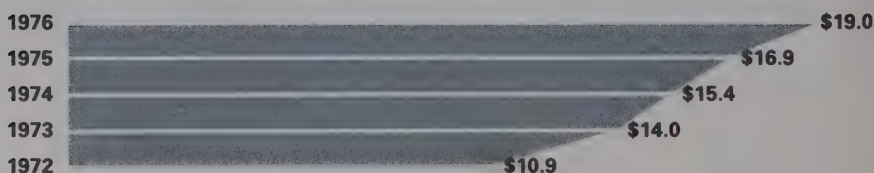
Cost of goods sold decreased \$13.2 million in fiscal 1976 because principal raw materials were purchased at significantly lower costs. In fiscal 1975, the cost of goods sold was above fiscal 1974 because of much higher raw material costs. Costs of labor, packaging, and distribution increased in both years. In addition, depreciation expenses and maintenance and repair expenses have increased in both years, primarily as a result of capital additions and a higher level of business activity, respectively.

Selling, general and administrative expenses were up 18 percent in fiscal 1976, to \$304 million, following a 19 percent increase in the prior year.

Advertising and Merchandising Expenses Of the fiscal 1976 increase, more than half was due to a 23 percent increase in consolidated advertising and merchandising, including consumer couponing, to provide continuing support for major brand-name franchises and market shares. Sixty-two percent of the fiscal 1975 increase, or \$25.8 million, was in advertising and merchandising expenses for domestic grocery products, to support established and new products in major categories — particularly pet foods.

Research and Development Expenses Research and development expenditures increased \$2.1 million in fiscal 1976. In fiscal 1975, R & D expenses were up 10 percent. These increases are consistent with Quaker's continuing emphasis on technical research and new product development. Not included in these figures are costs of market research or continuing quality assurance procedures performed in manufacturing operations.

Research and Development Expenses (Millions of Dollars)



Other expenses (Marx sale) A major expense item in fiscal 1976 was the pre-tax write-off of \$23.2 million, equivalent to 57 cents a share, in connection with the sale of substantially all of the assets of the U.S. and Canadian Marx businesses, and the stock in Marx Hong Kong operations to a U.S. subsidiary of Dunbee-Combex-Marx, Ltd., of London, England. Quaker received \$8.1 million in cash on the sale date, April 15, and D-C-M guaranteed further payment of \$10.0 million, due January, 1977, through January, 1982. Prior to the sale, operating losses in fiscal 1976 (loss before deduction of interest and income taxes) of \$12.2 million were incurred on the operations that were sold. In fiscal 1975 operating losses of the operations that were sold amounted to \$13.2 million, including about \$5 million of write-downs related to closing facilities and eliminating certain toy lines. The operations sold had sales of \$42.8 million in 1976 (prior to the sale) and \$64.3 million in 1975. Quaker's 56 percent interest in Plastimarx, the successful Marx Mexican subsidiary, was not included in the sale, and now operates as part of the Fisher-Price Toys Division.

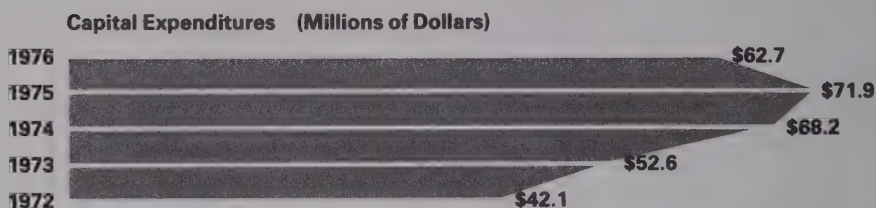
Net interest expense declined 49% in fiscal 1976 to \$13.4 million, reflecting lower working capital requirements, lower interest rates, and the full-year effect of the \$50 million preference stock offering that was sold in May, 1975. This contrasts with the Company's experience in fiscal 1975, when expanded borrowing needs and higher interest rates resulted in an increase in net interest expense of 25 percent, to \$26.4 million.

Tax rate in fiscal 1976 is 52.1 percent, down from 53.9 percent in the prior year, primarily because of a change of mix in earnings from domestic and international sources. The fiscal 1974 tax rate was 47.9 percent. The fiscal 1975 tax rate was higher than the 1974 rate due to the absence of a \$1.4 million gain from a tax-free disposition of land and lower tax-free earnings in Conservas Coqueiro, S.A.

Net income increased 71% in fiscal 1976 to \$53.1 million. In fiscal 1975, it was \$31 million, down 22 percent from the prior year.

The fiscal 1976 net income is after an \$11.9 million after-tax write-off related to the Marx sale and a \$600,000 after-tax charge related to the change to the LIFO method for pricing domestic Chemicals Division inventories. Fiscal 1975 net income was after a \$4 million after-tax charge to cover the costs of eliminating certain toy lines and a consolidation of facilities.

Capital expenditures in the last five years have totalled \$297.5 million. The new chemicals plant in Bayport, Texas, was a principal area of capital expense in fiscal 1975 and 1976. In fiscal 1977, an increase in capital expenditures is presently projected, with spending expected to be dispersed broadly throughout the business.



Dividends The Company's quarterly common share dividend was increased to 21 cents a share, effective with the payment on October 20, 1975. This was the ninth consecutive year in which the dividend was raised.

Financing Under arrangements with the Gulf Coast Waste Disposal Authority, Houston, Texas, \$15 million in solid waste disposal revenue bonds were issued. Of these, \$12 million are due in 2006 and carry an interest rate of 6½%, and \$3 million are due in 1991 with an interest rate of 5½%. The proceeds provide financing for the acquisition and construction of solid waste disposal facilities at the Company's new chemical plant in Bayport, Texas.

The Company's \$50 million revolving credit agreement was increased to \$75 million, and the maturity was extended to June 30, 1979. The Company also has domestic bank lines of credit totaling approximately \$100 million. None of the \$175 million bank facilities is currently in use. During the year, a \$20.2 million long-term note, due 1980, was prepaid.

Quaker's non-U.S. subsidiaries have credit facilities totaling \$68 million. At June 30, 1976, \$43 million of these facilities were not being used.

Quarterly Financial Data (Unaudited)

Year Ended June 30

Millions of Dollars
Except Per Share

	First Quarter (Sept. 30)	Second Quarter (Dec. 31)	Third Quarter (Mar. 31)	Fourth Quarter (Jun. 30)	Full Fiscal Year
1976					
Net sales	\$385.7	\$394.8	\$356.3	\$336.2	\$1,473.0
Cost of goods sold	263.8	271.6	241.2	239.6	1,016.2
Gross profit	<u>\$121.9</u>	<u>\$123.2</u>	<u>\$115.1</u>	<u>\$ 96.6</u>	<u>\$ 456.8</u>
Net income	\$ 22.0	\$ 4.9	\$ 15.9	\$ 10.3	\$ 53.1
Preferred and preference dividends	1.3	1.3	1.3	1.3	5.2
Net income available for common	<u>\$ 20.7</u>	<u>\$ 3.6</u>	<u>\$ 14.6</u>	<u>\$ 9.0</u>	<u>\$ 47.9</u>
Income per common share	1.00	.18	.70	.43	2.31
Cash dividends declared per common share	.21	.21	.21	.21	.84
Market price range per common share	20 $\frac{1}{8}$ — 15	27 $\frac{1}{4}$ — 16 $\frac{7}{8}$	28 $\frac{3}{8}$ — 22 $\frac{3}{4}$	27 $\frac{3}{8}$ — 22 $\frac{3}{4}$	28 $\frac{3}{8}$ — 15

1975

Net sales	\$344.0	\$372.7	\$328.3	\$344.0	\$1,389.0
Cost of goods sold	261.2	282.5	239.9	245.8	1,029.4
Gross profit	<u>\$ 82.8</u>	<u>\$ 90.2</u>	<u>\$ 88.4</u>	<u>\$ 98.2</u>	<u>\$ 359.6</u>
Net income	\$ 8.6	\$ 5.4	\$ 7.8	\$ 9.2	\$ 31.0
Preferred and preference dividends	.1	.1	.1	.8	1.1
Net income available for common	<u>\$ 8.5</u>	<u>\$ 5.3</u>	<u>\$ 7.7</u>	<u>\$ 8.4</u>	<u>\$ 29.9</u>
Income per common share	.41	.26	.37	.41	1.45
Cash dividends declared per common share	.20	.20	.20	.20	.80
Market price range per common share	24 $\frac{3}{8}$ — 12 $\frac{1}{2}$	16 $\frac{1}{4}$ — 11	18 $\frac{1}{2}$ — 12 $\frac{3}{8}$	20 $\frac{1}{2}$ — 14	24 $\frac{3}{8}$ — 11

Sales and Operating Income by Area

Millions of Dollars					
Year ended June 30	1976	1975	1974	1973	1972
Sales and Operating Income					
Grocery Products Area					
U.S. and Canadian	\$759.8	\$735.0	\$628.9	\$528.1	\$484.1
	88.9	50.3	48.3	51.1	43.5
International	256.6	224.6	197.0	133.9	106.7
	17.7	11.5	14.0	6.8	5.3
Total Grocery Products Area	1016.4	959.6	825.9	662.0	590.8
	106.6	61.8	62.3	57.9	48.8
Diversified Businesses Area					
Toys and Crafts	247.5	243.5	270.1	224.7	116.8
	(6.4)^(A)	3.5 ^(B)	25.4	31.9	22.8
Chemicals	104.3	97.2	70.7	56.2	44.9
	11.8	22.1	8.5	5.8	4.6
Institutional Foods and Restaurants	104.8	88.7	60.6	47.9	42.7
	12.3	6.3	1.4	.9	1.0
Total Diversified Businesses Area	456.6	429.4	401.4	328.8	204.4
	17.7	31.9	35.3	38.6	28.4
Total Sales	1473.0	1389.0	1227.3	990.8	795.2
Total Operating Income	124.3	93.7	97.6	96.5	77.2
Less interest expense—net	13.4	26.4	21.1	11.0	6.6
Income before income taxes	\$110.9	\$ 67.3	\$ 76.5	\$ 85.5	\$ 70.6

Sales figures—Black ink

Operating income figures—Blue ink

(A) After a \$23.2 million pre-tax write-off provision resulting from the April 1976 sale of the U.S., Canadian and Hong Kong operations of the Marx Toys Division (equivalent to \$.57 per share).

(B) After pre-tax toy division charges of \$6.0 million related to the elimination of certain toy lines and the consolidation of facilities (equivalent to \$.19 per share).

The Quaker Oats Company and Subsidiaries

Consolidated Statements of Income and Reinvested Earnings

Thousands of Dollars

Year Ended June 30	1976	1975
Net Sales	\$ 1,473,052	\$ 1,389,013
Cost of goods sold	<u>1,016,220</u>	<u>1,029,355</u>
Gross profit	<u>456,832</u>	<u>359,658</u>
Selling, general and administrative expenses	304,037	256,834
Interest expense — net	13,426	26,441
Other expense	<u>28,483</u>	<u>9,090</u>
Income Before Income Taxes	110,886	67,293
Provision for income taxes	<u>57,793</u>	<u>36,256</u>
Net Income	53,093	31,037
Preferred and preference dividends	5,206	1,103
Net Income Available for Common	<u>\$ 47,887</u>	<u>\$ 29,934</u>
Per Common Share:		
Net income	\$2.31	\$1.45
Dividends declared	\$.84	\$.80
Average Common Shares Outstanding	20,711,092	20,699,008
Reinvested Earnings:		
Balance beginning of year	\$ 221,710	\$ 208,336
Net income	53,093	31,037
Dividends — preferred stock	(426)	(426)
— preference stock	(4,780)	(677)
— common stock	(17,400)	(16,560)
Balance end of year	<u>\$ 252,197</u>	<u>\$ 221,710</u>

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet

Assets

	Thousands of Dollars	
June 30	1976	1975
Current Assets:		
Cash and marketable securities	\$ 77,869	\$ 17,607
Receivables (less allowances of \$6,598 and \$6,696, respectively)	139,184	144,351
Inventories	198,206	188,703
Prepaid expenses	9,562	7,010
Current assets	<u>424,821</u>	<u>357,671</u>
Other Receivables and Investments	13,633	5,385
 Property, Plant and Equipment, at cost:		
Land	8,801	9,506
Buildings and improvements	148,759	148,877
Machinery and equipment	358,800	333,040
	<u>516,360</u>	<u>491,423</u>
Less accumulated depreciation	142,772	133,237
Properties — net	<u>373,588</u>	<u>358,186</u>
 Intangible Assets:		
Excess of cost over net assets of acquired businesses, less amortization	40,188	37,907
Patents, trademarks and designs, less amortization	2,717	5,913
	<u>\$854,947</u>	<u>\$765,062</u>

See accompanying notes to consolidated financial statements.

The Quaker Oats Company and Subsidiaries

Liabilities and Shareholders' Equity

	Thousands of Dollars	
June 30	1976	1975
Current Liabilities:		
Short-term debt	\$ 46,240	\$ 28,528
Current maturities of long-term debt	2,030	678
Accounts payable and accrued expenses	122,246	108,013
Income taxes payable	33,179	6,815
Dividends payable	5,655	4,924
Current liabilities	<u>209,350</u>	<u>148,958</u>
Long-term Debt	148,668	158,283
Other Liabilities	15,579	10,107
Deferred Income Taxes	49,599	46,967
Shareholders' Equity:		
Preferred, \$50 par value, \$3 cumulative convertible, authorized 147,553 and 147,836 shares, respectively; issued 141,821 and 142,104 shares, respectively	7,091	7,105
Preference, without par value, \$100 stated value, \$9.56 cumulative, authorized 1,500,000 shares; issued 500,000 shares	50,000	50,000
Common, \$5 par value, authorized 35,000,000 shares; issued 20,979,469 and 20,948,922 shares, respectively	104,897	104,745
Additional paid-in capital	23,193	22,814
Reinvested earnings	252,197	221,710
	<u>437,378</u>	<u>406,374</u>
Less treasury common stock, at cost	5,627	5,627
Shareholders' equity	<u>431,751</u>	<u>400,747</u>
	<u>\$854,947</u>	<u>\$765,062</u>

Consolidated Statement of Changes in Financial Position

	Thousands of Dollars	
Year Ended June 30	1976	1975
Sources of Funds:		
Operations		
Net income	\$ 53,093	\$ 31,037
Depreciation and amortization	34,832	31,195
Deferred income taxes	2,632	10,456
Loss on sale of Marx non-current assets	9,700	—
Total from operations	<u>100,257</u>	<u>72,688</u>
Issuance of 500,000 shares of preference stock	—	50,000
Proceeds from new long-term debt	16,050	28,250
Increase in other long-term liabilities	5,472	1,911
Proceeds from sale of Marx non-current assets	6,646	—
Sales of properties — other	2,510	3,411
Decrease in receivables	5,167	15,778
Increase in accounts payable and accrued expenses	14,233	16,379
Increase (decrease) in income taxes payable	26,364	(633)
Increase (decrease) in short-term debt	17,712	(86,167)
Other — increase (decrease) — net	438	(1,283)
Total funds provided	<u>194,849</u>	<u>100,334</u>
Uses of Funds:		
Additions to properties	62,709	71,899
Cash dividends paid	22,606	17,663
Decrease in long-term debt	25,665	41,394
Excess of cost over net current assets of acquired businesses	5,856	505
Increase (decrease) in inventories	9,503	(36,469)
Increase (decrease) in other receivables and investments	8,248	(583)
Total funds used	<u>134,587</u>	<u>94,409</u>
Net increase in cash and marketable securities	<u>\$ 60,262</u>	<u>\$ 5,925</u>

See accompanying notes to consolidated financial statements.

The Quaker Oats Company and Subsidiaries

Notes to Consolidated Financial Statements

Consolidation The consolidated financial statements include The Quaker Oats Company and all subsidiaries. All significant intercompany accounts and transactions are eliminated. Investments in 20% to 50% owned companies are stated on the equity basis.

Currency Translation Non-U.S. currency items are translated into U.S. dollars at year-end exchange rates for assets and liabilities and average annual exchange rates for income items, except properties and intangibles and related depreciation and amortization, which are translated at rates in effect at the time of acquisition.

Unrealized translation gains are credited to a reserve, except to the extent that they offset previously recorded losses; unrealized losses in excess of previously established reserves are charged to income. Gains and losses on forward exchange contracts are recognized in income upon settlement.

The Company will adopt the provisions of Financial Accounting Standards Board Statement No. 8 next fiscal year, as required. The provisions of the Statement, if applied to 1976 and 1975, would have had no material effect on net income.

Intangibles Excess of cost over net assets of acquired businesses, including \$27,468,000 related to acquisitions prior to November 1, 1970 (principally Fisher-Price Toys, Inc.), represents the amounts paid in excess of the fair values of the net assets of such businesses, less amortization. Such costs are considered to represent continuing values and are adjusted if reduction of the continuing values of underlying businesses is indicated. As required by current accounting rules, all such costs resulting from acquisitions after October 31, 1970, are amortized over periods not in excess of 40 years. Amortization for 1976 and 1975 was \$1,345,000 and \$808,000, respectively.

Costs incurred in acquiring patents, trademarks and designs are amortized on a straight-line basis over their estimated useful lives. Amortization for 1976 and 1975 was \$523,000 and \$811,000, respectively.

Inventories Inventories are priced at the lower of cost (first-in, first-out for toys and crafts products, last-in, first-out for domestic chemical products, and principally average annual cost for other products) or market. Inventory costs include material, labor and factory overhead.

In the fourth quarter of 1976, the Company changed its method of pricing domestic Chemical Division inventories from average annual cost to last-in, first-out (LIFO). This change was made retroactive to the beginning of the fiscal year. The effect of the change was to reduce net income by 3 cents a share.

The following inventories were used in computing costs of goods sold:

	Thousands of Dollars	
	1976	1975
Finished goods	\$116,948	\$ 101,222
Grain and materials	70,309	74,767
Supplies	10,949	12,714
	<u>\$198,206</u>	<u>\$ 188,703</u>

Depreciation and Properties Depreciation is computed using the straight-line method, which is designed to recover the cost of the properties over their estimated useful lives. The rates used were:

Buildings and improvements	2% to 6%
Machinery and equipment	4% to 20%
Automobiles and trucks	Various
Miscellaneous equipment, office furniture and fixtures	10% to 20%

Accelerated depreciation methods are used for income tax purposes. Depreciation for tax purposes exceeds book depreciation, and deferred taxes are provided.

Maintenance and repairs are charged to expense as incurred. Significant replacements and betterments are capitalized.

The composite method is used for depreciation, and only abnormal gains and losses on sales or abandonments of property are included in income.

Research and Development Costs are expensed as incurred.

Advertising Costs are expensed as incurred.

Investment Tax Credits Investment tax credits are deferred and amortized over the estimated useful lives of the related assets. At June 30, 1976, \$11,310,000 of deferred tax credits are included in deferred income taxes.

Undistributed Non-U.S. Earnings Except for minor amounts, no federal income taxes have been provided on the undistributed net income of non-U.S. subsidiaries since these amounts are expected to be permanently invested in those countries.

Pension Plans The provision for pensions charged to income each year is sufficient to cover normal costs of the plans of the Company and its subsidiaries and, for the principal plans, amortization of prior-service costs over 40 years or less. Effective January 1, 1976, the Company made certain amendments to its pension plans, principally to reflect the provisions of the Pension Reform Act of 1974. These changes did not have a material effect on pension costs, which amounted to \$9,389,000 in 1976 and \$9,001,000 in 1975. Pension funds are in excess of the actuarially computed value of vested benefits.

Income Per Share Net income per common share is based on the weighted average shares outstanding. Dilution resulting from the exercise of stock options presently outstanding and conversion of preferred stock is not significant.

Non-U.S. Operations Summarized financial information for non-U.S. operations follows:

	Thousands of Dollars	
	1976	1975
Assets:		
Current assets	\$134,877	\$120,420
Property, plant & equipment — net	64,038	60,894
Other assets	19,358	16,398
	<u>\$218,273</u>	<u>\$197,712</u>
Less:		
Current liabilities	\$ 72,371	\$ 63,975
Other liabilities	18,441	22,753
	<u>\$ 90,812</u>	<u>\$ 86,728</u>
Total net assets	<u>\$127,461</u>	<u>\$110,984</u>
Net assets:		
Canada	\$ 23,495	\$ 21,366
Europe	62,450	45,186
Latin America and Pacific	41,516	44,432
Total	<u>\$127,461</u>	<u>\$110,984</u>
Net sales:		
Canada	\$ 98,209	\$ 83,939
Europe	201,856	181,982
Latin America and Pacific	122,648	107,749
Total	<u>\$422,713</u>	<u>\$373,670</u>
Reinvested earnings	<u>\$ 67,805</u>	<u>\$ 60,517</u>

In 1976, the exchange and translation loss amounted to \$850,000 and was charged to income. The reserve for unrealized translation gains, included in other liabilities, decreased by \$74,000 during the year and at June 30, 1976 was \$1,228,000.

In 1975 the net exchange and translation loss amounted to \$2,008,000 and was charged to income. The reserve for unrealized translation gains, included in other liabilities, increased by \$12,000 during the year and at June 30, 1975 was \$1,302,000.

Acquisitions During fiscal 1976, the Company acquired the remaining interest in its French joint venture, Quaker France S.A., for approximately \$4,262,000 in cash in a purchase transaction. The results of operations of this business, which are not material, are included in the Consolidated Statement of Income. The related excess of cost over fair value of net assets acquired is \$3,592,000.

Preferred Stock Each \$3 cumulative preferred share, redeemable by the Company at \$58 per share, is convertible at the holder's option into 2.475 shares of common stock. There were 283 shares of preferred stock converted into common during 1976 and no shares were converted during 1975. At June 30, 1976, there were 351,007 shares of common stock reserved for conversion of the \$3 cumulative preferred stock.

Preference Stock On May 29, 1975, the Company issued 500,000 shares of \$9.56 cumulative preference stock with a stated value of \$100 per share. This stock is redeemable, at the option of the Company, in whole or in part at prices decreasing from \$109.56 per share currently to \$100 after July 19, 2000, except that until July 20, 1980, such redemption cannot be made from the proceeds of indebtedness or the issuance of stock other than common stock having a cost of less than 9.56%. Each year, commencing on July 20, 1981, the Company must make payments to a sinking fund in an amount adequate to retire a minimum of 20,000 shares (maximum 40,000 shares) of preference stock at \$100 per share, plus accrued dividends to the redemption date. An additional 1,000,000 shares of preference stock, without par value, is authorized but unissued.

Common Stock Changes in common stock, additional paid-in capital and treasury common stock during 1975 and 1976 are summarized as follows:

Thousands of Dollars					
	Common Stock		Add'l. Paid-in Capital	Treasury	
	Shares	Amts.		Common Stock Shares	Amts.
Balance, June 30, 1974	20,948,922	\$104,745	\$23,882	249,914	\$5,627
Issuance costs of preference stock	—	—	(1,068)	—	—
Balance, June 30, 1975	20,948,922	104,745	22,814	249,914	5,627
Common stock issued for exercise of options and for conversions of preferred stock	30,547	152	379	—	—
Balance, June 30, 1976	20,979,469	\$104,897	\$23,193	249,914	\$5,627

Stock Options At June 30, 1976, 763,838 unissued shares of common stock were reserved for issuance upon the exercise of outstanding stock options, and an additional 97,548 unissued shares were available as of that date for granting additional options. Options are granted at not less than fair market value at date of grant. Option prices range from \$13.13 to \$42.82 per share. During 1976, options for 10,985 shares were granted at a price of \$25.19 per share, 29,849 options were exercised, and options for 167,521 shares were terminated. During 1975, options for 411,125 shares were granted at prices ranging from \$13.13 to \$15.06 per share, no options were exercised and options for 128,853 shares were terminated.

Reinvested Earnings Under the most restrictive terms of the various note agreements in effect at June 30, 1976, \$176,391,000 of reinvested earnings, as of June 30, 1976, was not available for payment of cash dividends and/or certain other distributions to preferred, preference and common shareholders; and minimum working capital of \$175,000,000 must be maintained.

Cash and Marketable Securities

	Thousands of Dollars	
	1976	1975
Cash	\$ 1,363	\$ 13,174
Time deposits and certificates of deposit	66,173	2,222
Marketable securities	10,333	2,211
	<u>\$ 77,869</u>	<u>\$ 17,607</u>

Marketable securities are stated at cost, which approximates market.

Short-Term Debt

	Thousands of Dollars	
	1976	1975
Notes payable to banks—		
Non-U.S. subsidiaries	\$24,833	\$ 23,506
Commercial paper—		
Dealer placed	—	—
Master trust notes	21,407	5,022
	<u>\$46,240</u>	<u>\$ 28,528</u>
Weighted average interest rates on debt outstanding at end of year —		
Notes payable to banks—non-U.S.	12.5%	11.7%
Commercial paper	5.9%	6.1%
Weighted average interest rates on debt outstanding during the year —		
Notes payable to banks—non-U.S. (computed on quarter-end balances)	11.5%	11.7%
Commercial paper (computed on daily balances)	6.2%	10.3%
Weighted average amount of debt outstanding during the year	\$54,816	\$111,000
Maximum month-end balance during the year	\$74,389	\$169,000

Long-Term Debt

	Thousands of Dollars	
	1976	1975
Solid waste disposal revenue bonds	\$ 15,000	\$ —
7.70% sinking fund debentures, \$1,800,000 due annually from 1977 through 2001	50,000	50,000
7.80% notes, \$3,700,000 due annually from 1980 through 1989 and \$3,800,000 due annually from 1990 through 1994	56,000	56,000
8¾% note, \$1,665,000 due annually from 1980 through 1994	25,000	25,000
Note payable, due 1980	—	20,188
Capitalized lease obligations	1,729	1,684
Obligations of non-U.S. subsidiaries	2,969	6,089
	<u>\$150,698</u>	<u>\$158,961</u>
Less: Current maturities	2,030	678
	<u>\$148,668</u>	<u>\$158,283</u>

Under arrangements with the Gulf Coast Waste Disposal Authority, Houston, Texas, \$15,000,000 in solid waste disposal revenue bonds were issued in June, 1976. Of these, \$3,000,000 carry an interest rate of 5½% and the remaining \$12,000,000 have an interest rate of 6½%. The proceeds provide financing for the acquisition and construction of solid waste disposal facilities at the Company's new chemical plant in Bayport, Texas. The 5½% bonds are due 1991 and may be called on any interest payment date on or after May 1, 1986, at rates decreasing from 103% to 100% on May 1, 1991. The 6½% bonds are subject to sinking fund redemptions of \$1,000,000 from 2000 to 2002, and additional redemptions increasing by \$500,000 per year from 2003 to 2006; optional redemptions may be made on any interest payment date on or after May 1, 1986, at rates decreasing from 103% to 100% on May 1, 1992.

The 7.70% debentures may be called at any time at prices decreasing from 106.2% currently to 100% after June 15, 1996, except that, until June 15, 1981, such redemption cannot be made from the proceeds of any refunding operation having an interest cost of less than 7.70%.

The 7.80% notes may be called at any time at prices decreasing from 107.8% currently to 100% in 1994, except that, until April 1, 1984, no prepayment may be made from the proceeds of any refunding operation by the application of borrowed funds.

The 8¾% note may be called at any time at prices decreasing from 108.3% currently to 100% after July 1, 1993, except that, until July 1, 1984, no prepayment may be made from the proceeds of any refunding operation having an interest cost of less than 8¾%.

Aggregate required payments for fiscal years 1977 through 1981 on long-term debt are: \$2,030,000, \$2,366,000, \$2,380,000, \$6,713,000 and \$7,482,000, respectively.

The Company has a revolving credit agreement, none of which has been utilized, that provides for \$75,000,000 in either domestic or Eurodollar borrowings at the Company's option and expires June 30, 1979. The agreement requires a commitment fee of ½ of 1% for any unused portion.

The Company, in addition to the unused \$75,000,000 revolving credit agreement, has approximately \$100,000,000 available in unused domestic bank lines of credit to meet general corporate purposes. The Company's non-U.S. subsidiaries had additional unused lines of credit of approximately \$43,000,000 at June 30, 1976.

The Company has informal arrangements with certain banks to maintain balances in compensation for credit facilities. These compensating balance arrangements, which totalled about \$6,180,000 at June 30, 1976, are based on the average annual amount on deposit according to bank records and impose no restrictions upon the Company's withdrawal of funds. At certain other banks, compensation for credit facilities is on a fee basis.

Leases The Company and its subsidiaries lease certain equipment and operating properties under non-cancellable leases which expire at various dates through 2062. Certain of these leases are non-capitalized financing leases as defined by the Securities and Exchange Commission. The present value of non-capitalized financing leases and its effect on net income are not significant. Subleases and contingent rentals also are not significant.

Total rental expense for 1976 and 1975 was:

	Thousands of Dollars	
	1976	1975
Non-capitalized financing leases	\$ 2,394	\$ 1,476
Other	12,932	12,413
	<u>\$15,326</u>	<u>\$13,889</u>

Future minimum annual rentals on non-cancellable leases in effect at June 30, 1976 are:

Fiscal Years	Financing (Primarily Office Equipment)	Thousands of Dollars			
		Operating		Other	Total
		Buildings	Distribution Equipment		
1977	\$2,344	\$5,434	\$775	\$156	\$8,709
1978	1,440	4,821	527	149	6,937
1979	151	4,389	320	140	5,000
1980	38	4,317	269	15	4,639
1981	18	4,213	269	13	4,513
1982-1986	67	23,852	166	43	24,128
1987-1991	65	5,476	—	43	5,584
1992-1996	65	3,961	—	43	4,069
Thereafter	818	1,113	—	54	1,985

Provision For Income Taxes

	Thousands of Dollars	
	1976	1975
Currently payable —		
Federal	\$33,724	\$15,094
State	4,969	2,337
Non-U.S.	16,468	8,369
Deferred — (primarily federal taxes related to depreciation and, in 1976, effect of the Marx sale)	(2,200)	7,881
Deferred investment tax credit — net	4,832	2,575
	<u>\$57,793</u>	<u>\$36,256</u>

The provision for income taxes varied from the "expected" tax expense computed at 48% of income before income taxes, as follows:

	Thousands of Dollars			
	1976		1975	
	Amount	% of Pretax Income	Amount	% of Pretax Income
Computed "expected" tax expense	\$53,225	48.0%	\$32,301	48.0%
State and local income taxes, net of federal income tax benefit	2,806	2.5	1,497	2.2
Non-U.S. tax rate differential	1,965	1.8	1,839	2.7
Miscellaneous items—net	(203)	(.2)	619	1.0
Actual tax expense	<u>\$57,793</u>	<u>52.1%</u>	<u>\$36,256</u>	<u>53.9%</u>

The change in the mix of domestic and international earnings was the principal reason for the lower effective income tax rate in 1976 compared to 1975.

Other Expense

	Thousands of Dollars	
	1976	1975
Commitment fees for credit facilities	\$ 432	\$ 408
Net exchange and translation losses	850	2,008
Toy division charges	23,200	6,052
Other—net	4,001	622
Total	<u>\$28,483</u>	<u>\$ 9,090</u>

The 1976 toy division charges relate to the April 15, 1976, sale of substantially all of the assets of the Company's U.S. and Canadian Marx Toys business, as well as the stock of Marx Hong Kong operations. After related income tax benefits of \$11,300,000, net income was reduced by \$11,900,000, equivalent to \$.57 per common share. (Complete details of the Marx sale are on page 27.) The 1975 toy division charges are related to the elimination of certain toy lines and the consolidation of facilities. After related income tax benefits of \$2,019,000, net income was reduced \$4,033,000, equivalent to \$.19 per common share.

Interest Expense — Net

	Thousands of Dollars	
	1976	1975
Interest expense on long-term debt	\$12,092	\$16,532
Interest expense — other	5,186	11,622
Interest income on marketable securities, including time deposits and certificates of deposit	(2,719)	(1,141)
Interest income — other	(1,133)	(572)
	<u>\$13,426</u>	<u>\$26,441</u>

Supplementary Income Statement Information

	Thousands of Dollars	
	1976	1975
Maintenance and repairs	\$34,989	\$28,977
Depreciation	\$32,964	\$29,576
Taxes, other than income		
Real estate and personal property	\$ 5,053	\$ 4,315
Payroll	14,760	13,377
Other	2,146	2,427
Total	<u>\$21,959</u>	<u>\$20,119</u>
Advertising media and production costs	\$57,800	\$50,611
Research and development	\$18,964	\$16,864

Litigation The Federal Trade Commission, in a complaint filed on April 26, 1972, alleged that the ready-to-eat cereal industry is concentrated in and controlled by four industry members, including the Company, which members have diminished competition by avoiding price competition and by raising entry barriers through various practices such as brand proliferation, excessive and misleading advertising, exclusionary shelf-space programs, and acquisitions. The Federal Trade Commission has proposed an order requiring the other three respondents (but not the Company) to divest certain properties and license certain trademarks to other manufacturers, and prohibiting all of the respondents (including the Company) from acquiring other cereal manufacturers for twenty years and from providing shelf-space programs to customers. The Company has denied the charges and trial has recently begun. In the opinion of the Company's Vice President and Special Counsel, the Company has meritorious defenses to the allegations in the complaint. The Company believes that the litigation will have no material adverse effect on its business.

Auditors' Report

To the Shareholders of The Quaker Oats Company:

We have examined the consolidated balance sheet of The Quaker Oats Company (a New Jersey corporation) and Subsidiaries as of June 30, 1975, and June 30, 1976, and the related consolidated statements of income, reinvested earnings and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of The Quaker Oats Company and Subsidiaries as of June 30, 1975, and June 30, 1976, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the periods.

Arthur Andersen & Co.

Chicago, Illinois

August 25, 1976

Corporate Headquarters

Merchandise Mart Plaza, Chicago, Illinois 60654

U.S. Transfer Agents and Registrars

The First National Bank of Chicago

One First National Plaza, Chicago, Illinois 60670

The Chase Manhattan Bank

One Chase Manhattan Plaza, New York, New York 10015

Dividend Disbursing Agent

The First National Bank of Chicago

Canadian Transfer Agent

National Trust Company, Limited

21 King Street East, Toronto 1, Ontario

Canadian Registrar

Crown Trust Company

302 Bay Street, Toronto, Ontario

Auditors

Arthur Andersen & Co.

69 West Washington Street

Chicago, Illinois 60602

(312) 346-6262

Shares Listed

New York Stock Exchange — Midwest Stock Exchange

Pacific Coast Stock Exchange — The Toronto Stock Exchange

The Stock Exchange, London — Amsterdam Stock Exchange

Ticker Symbol: OAT

Form 10-K

The Form 10-K, a separate annual report filed each year with the U.S. Securities and Exchange Commission, provides additional information about the Company. To obtain a copy without charge, please write or call the Office of the Secretary, The Quaker Oats Company, Merchandise Mart Plaza, Chicago, Illinois 60654, (312) 222-6751.



Members of the Board of Directors

Silas S. Cathcart

Chairman and Chief Executive Officer
Illinois Tool Works, Inc.
(Diversified Products)
Chicago, Illinois

*** John D'Arcy, Jr.**

Senior Vice President
Operations and Administration

Richard D. Harrison

President and Chief Executive Officer
Fleming Companies, Inc.
(Wholesale and Retail Foods)
Oklahoma City, Oklahoma

*** Augustin S. Hart, Jr.**

Senior Vice President
Planning

Dr. Thomas C. MacAvoy

President
Corning Glass Works
(Specialized Glass and Ceramic Products)
Corning, New York

*** Kenneth Mason**

Executive Vice President
Grocery Products

*** Archibald McClure**

Executive Vice President
Diversified Businesses

Donald E. Meads

Chairman and Chief Executive Officer
Certain-teed Products Corporation
(Building Materials)
Valley Forge, Pennsylvania

G. G. Michelson

Senior Vice President
Macy's New York
(Retail Merchandising)
New York City

Dr. Walter J. Salmon

Associate Dean for Educational Affairs
and Professor of Marketing
Harvard Business School
Boston, Massachusetts

Frank C. Schell, Jr.

Group Vice President

Gilbert H. Scribner, Jr.

President, Scribner & Co.
(Real Estate Brokerage, Management &
Appraisals)
Chicago, Illinois

*** Fred D. Stone**

Senior Vice President
Finance

*** Robert D. Stuart, Jr.**

President and Chief Executive Officer

*** Robert N. Thurston**

Senior Vice President
Corporate Affairs

Arthur M. Wood

Chairman and Chief Executive Officer
Sears, Roebuck and Co.
(Retail Merchandising, Insurance and
other services)
Chicago, Illinois

***Member of the Executive Committee**

Audit Committee

Mr. Wood, Chairman; Messrs. Meads
and Salmon

Compensation and Stock Option Committee

Mr. Scribner, Chairman;
Messrs. Cathcart and Harrison

Public Responsibility Committee

Mr. Cathcart, Chairman; Mrs. Michelson,
Dr. MacAvoy

Robert D. Stuart, Jr.
President and Chief Executive Officer

**Corporate
Staff**

John D'Arcy, Jr.
Senior Vice President—Operations and Administration

William A. Bales
Vice President—Corporate Purchasing

Thomas B. Bartel
Vice President—Corporate Personnel

Lawrence M. Baytos
Vice President—Employee Relations

Sam H. Flint
Vice President—Corporate Operations

Augustin S. Hart, Jr.
Senior Vice President—Planning

Kenneth J. Fedor
Vice President—Economics and Planning

James S. Van Pelt, Jr.
Vice President—Business Development

Fred D. Stone
Senior Vice President—Finance

Robert D. Guy
Vice President—Corporate Taxes

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Vice President and Treasurer

Herbert E. Trenning
Assistant Treasurer

Donald G. Wittmer
Corporate Controller

Robert N. Thurston
Senior Vice President—Corporate Affairs

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Vice President and General Counsel

Luther C. McKinney
Vice President, Special Counsel and
Corporate Secretary

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Assistant Secretary

Louis J. Mallardi, Jr.
Assistant Secretary

Joann A. Pitcher
Assistant Secretary

Howard J. Thomas, Jr.
Assistant Secretary

Frank C. Schell, Jr.
Group Vice President

**Grocery
Products Area** ***Kenneth Mason**
Executive Vice President
Grocery Products Area

Area Staff ***Frank J. Morgan**
Group Vice President
Grocery Products Operations

***Henry T. Chandler**
Vice President—Sales and Distribution

***Robert O. Nesheim**
Vice President
Research and Development

Paul R. Pearce
Vice President—Personnel

Lois I. Ross
Vice President—Consumer Services

Robert E. Smith
Vice President—Quality Assurance

Raymond C. Eggleston
Vice President and Controller

***Jack M. Young**
Vice President—Marketing Services

Dudley M. Ruch
Vice President—Marketing Research

Mitchell A. Seltzer
Vice President—Advertising
President, AdCom, Inc.

Joan G. Stark
Vice President and Media Director
AdCom, Inc.

**Area
Profit Centers** ***William D. Smithburg**
President—Foods Division

***Royce S. Ramsland**
Vice President—Purchasing,
Foods Division

George J. Yapp
Vice President—Operations,
Foods Division

***Richard H. Glantz**
President—Pet Foods Division

Hedric E. Rhodes
Vice President—Product Management,
Pet Foods Division

Herbert H. Johnson
Chairman of the Board
Wolf Brand Products

U. B. Shockley
President—Wolf Brand Products

***Paul E. Price**
Group Vice President
International Grocery Products

David R. Nogle
Vice President—Operations
International Grocery Products

***Anthony J. Dimino**
Vice President and Director
Mexican Grocery Products

***Ronald G. Lagden**
Vice President and Director
European Grocery Products

J. Byron Felter, Jr.
Vice President and Managing Director
Quaker Oats, Ltd., The United Kingdom

Jon K. Grant
President
The Quaker Oats Company of Canada

**Diversified
Businesses Area** *Archibald McClure
Executive Vice President
Diversified Businesses Area

***Leonard W. Steiger, Jr.**
President—Chemicals Division

Andrew P. Dunlop
Vice President and Scientific Advisor

James R. King
Vice President
Administration and Planning

William J. McKillip
Vice President
Research and Development

Robert F. Morgan
Vice President and
Director—Personnel

Robert W. Reardon
Vice President—Marketing

Kenneth J. Siegfried
Vice President—Business Development

Earl K. Stigger
Vice President and Controller

William C. Trotter
Vice President—Operations

***Alan R. Ryan**
President—Burry Division

John H. Horn
Vice President—Manufacturing

***Frederick D. Montgomery**
President—Magic Pan, Inc.

James J. Durkin
Vice President—Operations

Samuel T. Gentles
Vice President—Site Development

***Henry H. Coords**
President—Fisher-Price Toys Division

Harvey W. Busch
Vice President
Planning and Information Systems

James H. Frank
Vice President and Controller

Robert H. Hicks
Vice President
Research and Development

Norman G. Schuller
Vice President—Engineering

Charles J. Weinschneider
Vice President—Marketing

John Zahorjan
Vice President—Operations

***Lowell S. Fixler**
President—Needlecraft Division

Edward R. Cowell
Vice President—Manufacturing

Vincent W. Goeltz
Executive Vice President
Herrschners, Inc.

"If this business were to be split up, I would be glad to take the brands, trademarks, and goodwill, and you could have all the bricks and mortar.

"And I would fare better than you."

John Stuart

President 1922-1942

Chairman of the Board 1942-1956

Why?

An easy question to answer, especially now that we're celebrating the hundredth year of The Quaker Man trademark. On September 4, 1877, it was officially registered at the U.S. Patent Office as a symbol of the purity and quality of the oatmeal and other products made and sold by the company.

A lot has happened since then; the world has changed dramatically. Quaker has changed with the times, too, but what that first trademark represented in 1877 remains basically the same today.

Many other well known brands and trademarks accompany The Quaker Man now, each adding its own unique identity to other foods and product lines.

There's Aunt Jemima—warm, friendly, inviting all to enjoy the high-value foods that carry her name.

There's Fisher-Price, rugged quality toys that millions of children are raised on, to later hand down to younger brothers and sisters, or perhaps keep in the toy box for the grandchildren.

There's Life Cereal for the entire family, and Cap'n Crunch for the children. Celeste, for pizza abundant with flavor. And Burry cookies and crackers.

For pets, there are no better foods than Ken-L Ration and Puss 'n Boots.

Magic Pan Restaurants have distinctive flair, offering crepes filled with everything good to eat.

And specialty chemicals; and Needlecraft, to express individual creativity.

Around the world, consumers are not only familiar with many of our U.S. family of brands and trademarks, but also know Carlos V chocolate products in Mexico, Felix and Chunky pet foods in the United Kingdom, Kalas Flingor ready-to-eat cereal in

Scandinavia, Fido dog food in France, Frescavena oat-based beverages in Latin America, Pamper cat food in Canada, Coqueiro canned sardines in Brazil, Luv pet foods in Australia, and many, many more.

When you come right down to it, The Quaker Man and our other trademarks not only represent fine quality products, but also have identities of their own; they are among the oldest and most recognized commercial symbols in the world. The goodwill of customers and employees has made them so.

John Stuart was right.

We are proud of our plants, buildings, and equipment. But the real consumer value of our business rests in those fine respected names and symbols, beginning with The Quaker Man himself a hundred years ago.

New Aunt Jemima Frozen Pancake Batter, the market leader in its category, and the 72 oz. size of Quaker Oats, which makes this traditional favorite even more economical.



Traditional Fisher-Price quality is built into the new Freddy Bear for infants and the Play Family Hospital for preschoolers.

Children and parents love these ready-to-eat cereals from Quaker.



Ken-L Ration dog food and Puss 'n Boots cat food – known to family pets throughout the land.





International Grocery Products – including the leading chocolate business in Mexico, the principal sardine business in Brazil, and traditional Quaker Oats – a favorite around the world.



Harvest Crunch, similar to Quaker 100% Natural Cereal in the U.S., and Puss 'n Boots Bouchees de Choix (Flavor Morsels), leading products of The Quaker Oats Company of Canada.



Celeste frozen pizzas are abundant with flavor. There's a size and variety for everyone's taste.



Aunt Jemima Whole Wheat Pancake Mix and syrup – a delightful combination for any breakfast table.



Two new products for the family pets from Ken-L Ration and Puss 'n Boots.

Burys manufactures Girl Scout cookies and cookies and crackers for sale in selected area stores.

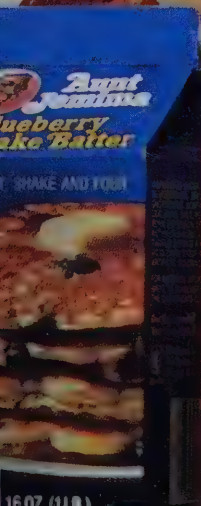


Cherokee, one of the new Latch Hook wallhanging yarn kits, and Poppy, a cameo stitchery kit, both from Needlecraft.



Some of our very important international pet food products: Felix and Chunky in the United Kingdom, Flora in Holland, and Ken-L Ration in Argentina.

The Quaker Oats Company
Merchandise Mart Plaza
Chicago, Illinois 60654



CELESTE CHEESE & MUSHROOM
Cashmere propolis added to most of our products.

New U.S. grocery products are pictured on the outside covers of this report.

Aunt Jemima Frozen Pancake Batter, Quaker Oatmeal Cookie Mix and Puss 'n Boots Fisherman's Platter cat food are available nationally. The others are presently in regional test markets. These products are discussed in a report by William D. Smithburg, Executive Vice President—U.S. Grocery Products, that begins on page 15.

Highlights of the Annual Shareholders' Meeting are on the facing page.

Reports to shareholders by the Chairman, the President and the three Executive Vice Presidents are reprinted beginning on page 2. These reports were followed by a question and answer period, which is summarized beginning on page 24.

The first interim report to shareholders, including an explanation of recent accounting changes, begins on page 26.

In September Robert D. Stuart, Jr. was elected Chairman and Chief Executive Officer, Kenneth Mason President and Chief Operating Officer, and several other officers assumed new responsibilities. A complete listing of corporate, area and divisional officers begins on page 35.

Annual Meeting Highlights

The Annual Meeting of Shareholders of The Quaker Oats Company was convened at 9:30 a.m. on Wednesday, November 10, 1976, at The Northern Trust Company in Chicago. Robert D. Stuart, Jr., Chairman and Chief Executive Officer, presided. Approximately four hundred shareholders were present.

Board of Directors

Fifteen incumbent directors were reelected to the Board. Their names and principal affiliations are shown on the inside back cover of this report.

Proposals

Directors' Proposal A regarding amendment of the 1971 Stock Option Plan — to increase the number of shares available and to grant limited stock appreciation rights — was approved by 92 percent of the shares voted (15,387,086 in favor; 1,330,715 opposed).

Directors' Proposal B regarding adoption of Part II of the Employee Stock Award Plan was approved by 98.2 percent of the shares voted (16,399,603 in favor; 296,588 opposed).

Directors' Proposal C regarding the appointment of Arthur Andersen & Co., Chicago, as independent auditors for the 1977 fiscal year was approved by 99.6 percent of the shares voted (16,632,733 in favor; 66,452 opposed).

A proposal by Mrs. Evelyn Y. Davis, a shareholder, to require that certain information about law firms retained by the Company be reported to shareholders, was defeated by 97.8 percent of the shares voted (345,820 in favor; 15,645,671 opposed).

The meeting was adjourned at 12:05 p.m.

At the Annual Meeting this year, Shareholders heard reports from Robert D. Stuart, Jr., Chairman and Chief Executive Officer, and Kenneth Mason, President and Chief Operating Officer, as well as brief comments from William D. Smithburg, Executive Vice President—U.S. Grocery Products; Frank J. Morgan, Executive Vice President—International Grocery Products; and Archibald McClure, Executive Vice President—Diversified Businesses. These reports, reprinted below, were followed by a question-and-answer period, which is summarized beginning on page 24.

Mr. Stuart

First we'd like to bring you up to date on our business as we see it at the present date.

You've all seen our annual report for the 1976 fiscal year, and you're familiar with the good financial results that were achieved.

Per-share earnings were up 13 percent over our previous record year in 1973, to \$2.31 a common share, even after allowing for the 57 cents write-off in connection with the sale of Marx Toys. Perhaps most important about that improvement is that it returned our earnings to the long-term trend lines that—barring unforeseen and uncontrollable future events—should be the base of continuing earnings progress.



First-Quarter Results

The better overall patterns of the last fiscal year have extended through the first quarter of this year. Just before this meeting convened this morning, we released our sales and earnings for the first fiscal quarter. Sales were up 2 percent to \$394.1 million, despite the fact that last year's first quarter included \$20.4 million in sales of the Marx Toys operations sold last April. Excluding last year's Marx business, consolidated sales were up 8 percent.

After reflecting some accounting changes, net earnings were \$25 million this year, compared to a pro forma \$24.3 million for the first quarter of last fiscal year. On a per-share basis, earnings were \$1.14 compared with a pro forma \$1.11 for the same period last year. It's important to note that last year's first quarter was very substantially higher than any prior first quarter in the Company's history.

Thus, we're pleased with this year's per-share results. While the increase amounts only to 3 percent, the comparison is with those unusually strong, record quarterly results of a year ago.

The accounting changes have to do with the method of translating international currency transactions and financial statements, now required of all business, and the way we value inventories and record certain advertising and merchandising expenses on an interim basis.

Reporting Quarterly Line-Of-Business Results

Beyond that, however, we believe that we have taken a very progressive step in reporting each quarter's results by major lines of business. Previously this sort of information was disclosed only at year-end in the annual report. From now on, starting with the first quarter this year, you'll be better able to track the progress of U.S. Grocery Products; International Grocery Products; Toys and Crafts (Fisher-Price and Needlecraft); Chemicals; and Institutional Foods and Restaurants (Burry and Magic Pan).

We believe this quarterly breakdown will be much more meaningful to shareholders and the investment community, and we certainly hope you agree.

Corporate Values

Now, in this same spirit of disclosure, of keeping you fully informed about our business, let me turn to a subject that has received a great deal of attention—the so-called “sensitive payments,” which have been revealed by some 400 international corporations.

We have very firm policies on ethical behavior at The Quaker Oats Company. When the subject of illegal or questionable payments to officials of foreign governments came up in some companies, we promptly re-examined our own policies and procedures and undertook an investigation of our own Company and its subsidiaries to be certain that Quaker policies were being adhered to. Directors were kept fully informed.

This investigation began in September, 1975, and was conducted by Mr. Luther C. McKinney, who is Group Vice President—Law and Public Affairs, and our Corporate Secretary. He interviewed our top management as well as the management of Quaker subsidiaries throughout the world. The period covered in the inquiry was approximately the last ten years.

I’m pleased to report that his investigation showed that, throughout the Company with only minimal exceptions, there has been no participation in questionable payments. Quaker’s basic policy about how we do business has been well understood. In several cases, in fact, managers exhibited considerable courage in rejecting demands for payments. Numerous requests for payoffs to minor government officials to obtain action to which we were legally entitled anyway were refused, resulting in one instance in physical abuse of a plant manager

and several instances of arbitrary delays in the processing of paper work necessary to obtain clearly justified government approvals.

During this same ten years of frequently refusing to be blackmailed, we did find a handful of payments of borderline propriety. But nothing has been discovered that is material to the company's financial position, either in terms of the size of payments, or the amount of business involved. All of these borderline payments occurred outside the United States and were in the nature of direct or indirect extortion by lesser governmental officials. No instance involved bribery by Quaker employees of officials. But I want to fully disclose to you what we did find.

The total amount was approximately \$114,000 over a ten-year period, based on historical exchange rates. Based on today's exchange rates, it would be a smaller amount. I must stress that we believe we have picked up every conceivable type of payment that might be questioned over the whole ten-year period. Four incidents involving extortion demanded to get legitimate price control papers processed in three countries account for the bulk of the total. The balance over the last decade consisted of a number of small gratuity-type payments, primarily in one country. All were made at the insistence of minor officials as a prerequisite to carrying out duties they were obligated to perform anyway, such as mail delivery, but which they refused to perform without receiving gratuities.

No off-book accounts were used, and these payments have no U.S. tax consequences. We are aware of no payments in the U.S. or, in fact, in most countries of the world.

Just to show how frustrating a problem this really is, let me give you an illustration. One of the demands refused was from a customs official in connection with the shipping of a transferred employee's furniture. As a consequence of our manager's refusal to pay, the furniture was stored in the open in a rainy climate, pending customs examination. It was ruined, but nevertheless taxed at a high value. And, of course, having an international manager's family furniture ruined is a distressing personal experience. But it's just one example of the harrassment that occurs.

Mr. McKinney's investigation is gratifying to me personally because it shows that in virtually every circumstance, even though our organization has expanded substantially in recent years, our Quaker managers and employees understood and have adhered to our traditional principles of honesty and fair dealing. The four incidents of extortion that I've reported were truly unusual circumstances, and relatively rare considering that we're talking about a time span of ten years in a large international business. This Company is very proud of its ethical business standards, which we consider to be one of our deepest and most enduring strengths.

I reaffirmed, on October 2, 1975, to all key managers the ethical business policy of The Quaker Oats Company. The policy is specific and unequivocal, and all managers are committed to it.

Management

Perhaps my greatest personal satisfaction in the last two months is the already evident effectiveness of our new top management team. As you know, we elected Ken Mason President and Chief Operating Officer in September.

In this and related organizational changes, we accomplished a number of things:

☐ We significantly strengthened our organization by making an extremely able and experienced officer — Ken Mason — responsible for company-wide operations.

☐ Two senior officers with distinguished, long service records, Jack D'Arcy and Gus Hart, moved up to Vice Chairmen, as part of orderly transition.

☐ Our three major business areas are headed by Executive Vice Presidents — Arch McClure, Frank Morgan and Bill Smithburg. You'll hear from each of them later this morning.

☐ Two Senior Vice Presidents — Fred Stone and Bob Thurston — have very broad corporate staff responsibilities.

☐ The average age of our three Executive Vice Presidents and two Senior Vice Presidents is now 45, and they have an average of more than twelve years service with the Company — important considerations for the management of the future. And just below them are a number of other extremely capable managers who have been given larger assignments.

I believe we now have the best management team in my experience at Quaker.

For all these reasons, I'm particularly pleased to introduce Ken Mason, our new President and Chief Operating Officer. He will review the operations of the business as a whole and comment on significant trends.

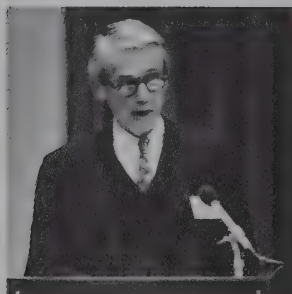
Mr. Mason

It's always a pleasure for me to discuss our business with you. I'm particularly delighted this morning because, with the exception of the Chemicals Division, which is experiencing some difficulties at the moment, our business appears to me to be in a very good position as we proceed into the remainder of fiscal 1977.

Three Business Areas

As you know, we have organized our business now into three specific areas headed by three Executive Vice Presidents — United States Grocery Products, International Grocery Products, and the Diversified Businesses Area, which includes Chemicals, Fisher-Price, Needlecraft, Burry and Magic Pan. First, let me give you an overview of our consolidated business as of the end of the first fiscal quarter.

The relative size of our three operating areas is shown on the chart on the facing page, which indicates their sales during the first quarter of the current fiscal year, with a percentage comparison to the same three months of last year. Overall, total corporate sales were 8 percent ahead of the record level of the first quarter last year.



Let me emphasize, by the way, that all of the data I'm using here today exclude figures for the Marx operations we sold last April. In other words, my discussion is on the basis of our continuing businesses.

First Quarter Sales

Fiscal 1977 vs. Fiscal 1976

(Millions of Dollars)

Three Months
Ended Sept. 30

	Amount	% Change
U.S. Grocery Products	\$184	+ 7%
International Grocery Products	87	+ 9%
Diversified Businesses	123	+ 8%*
Total Sales	\$394	+ 8%

*Results of the Marx Toys operations sold are not included.

The next chart looks at the three areas in terms of their operating income during the first quarter. Before discussing each of the three areas individually, let me point out that because we've made some changes in accounting, the comparisons I'm making are with our *pro forma* results for last year — in other words, as though we had kept last year's books the same way as this year's.

First Quarter Operating Income†

Fiscal 1977 vs. Fiscal 1976

(Millions of Dollars)

Three Months
Ended Sept. 30

	Amount	% Change
U.S. Grocery Products	\$ 29	+ 2%
International Grocery Products	8	+ 28%
Diversified Businesses	16	- 21%*
Total Operating Income	\$ 53	- 3%

*Results of the Marx Toys operations sold are not included.

†Operating income is defined as income before net interest expense and income taxes.

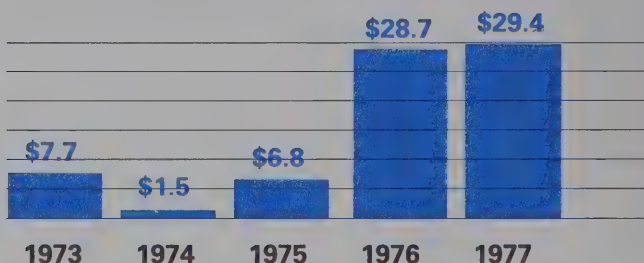
U.S. Grocery Products Area

Operating income of our largest business, U.S. Grocery Products, is up slightly over last year—and we are quite pleased with this result. Last year's first quarter was, as we stated at the time and as the chart indicates, an all-time record for U.S. Grocery Products—much higher than any first quarter in our history. This made it unlikely that this year's first quarter would equal, much less exceed, last year's. So the performance of our U.S. Grocery business in the first quarter is better than we expected, and is due mostly to two factors.

One, the strong sales performance of our breakfast cereals, frozen foods, and dog foods. Secondly, the fact that America's grain crop this year was of sufficient size for the second year in a row to maintain fairly steady prices in the commodity market. This, in turn, helped us to hold down the amount and frequency of price increases on our own products in the marketplace—a situation that I assure you pleases us every bit as much as it pleases consumers.

U.S. Grocery Products Area

First-Quarter Operating Income† (Millions of Dollars)



† Operating income is defined as income before net interest expense and income taxes.

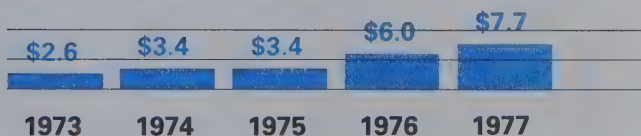
Whether the fairly strong sales trends we've been experiencing in the first quarter will continue throughout the year we simply cannot forecast reliably right now. At this point I would only say that our U.S. Grocery business is in good shape in terms of operating margins; we've increased our marketing expenditures from last year, particularly in pet foods;

and we have some interesting new products in various stages of development.

International Grocery Products Area

The \$7.7 million operating income for International Grocery Products is not only 28 percent ahead of last year's first quarter, but is an all-time high for any three-month period. Sales have been strong in local currencies, and there are good volume trends in pet foods in Europe, in chocolate products in Mexico, and in the sardine and corn goods businesses in South America.

International Grocery Products Area First-Quarter Operating Income† (Millions of Dollars)



†Operating income is defined as income before net interest expense and income taxes.

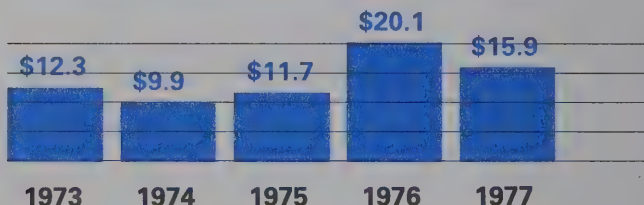
However, the key to profitability in the International Area at the moment is the effect fluctuating exchange rates are going to have on future profitability. The recent currency devaluations in Mexico and the United Kingdom did not dramatically affect first-quarter earnings, because new accounting rules require that inventories be revalued at the time they are sold, not at the time the value of the local currency changes. Therefore, the full extent to which our future sales and profits in Mexico and the United Kingdom will be affected will depend largely on the success of our marketing and pricing strategies in those countries from this point forward, and we won't know the outcome until later in the fiscal year. The currency devaluations are going to make last year's record earnings very hard to match. In Mexico, for example, earnings in pesos have to be at least twice as good as last year to translate into the same dollar profits.

Diversified Businesses Area

In the Diversified Businesses Area, we see operating income in the first quarter down 21 percent from last year's record. Most of this shortfall is in the Chemicals Division and, as you know, we've eliminated Marx losses both from our operations and from these charts.

Diversified Businesses Area*

First-Quarter Operating Income† (Millions of Dollars)



*Results of the Marx Toys operations sold are not included.

†Operating income is defined as income before net interest expense and income taxes.

Looking at sales, we see both Toys and Crafts and Institutional Foods and Restaurants running well ahead of last year, while Chemicals dollar sales are off 9 percent.

Diversified Businesses Area

First-Quarter Sales

Fiscal 1977 vs. Fiscal 1976

(Millions of Dollars)

Three Months
Ended Sept. 30

	Amount	% Change
Toys and Crafts	\$73.6	+ 12%*
Chemicals	23.9	- 9%
Institutional Foods and Restaurants	25.8	+ 19%
Total Diversified Businesses	\$123.3	+ 8%

*Results of the Marx Toys operations sold are not included.

In operating income, all three lines of business in the Diversified Businesses area are down in the first quarter, but only the decline in Chemicals is significant. The minus 36 percent figure for Institutional Foods and Restaurants involves only about half a million dollars, principally at Burry, and we're really quite pleased with

our overall trends in this area—as we are also with Toys and Crafts, which is in much better shape than a year ago when we still owned Marx Toys.

Diversified Businesses Area

First-Quarter Operating Income†

Fiscal 1977 vs. Fiscal 1976

(Millions of Dollars)

Three Months
Ended Sept. 30

	Amount	% Change
Toys and Crafts	\$14.9	– 3%*
Chemicals	.1	– 97%
Institutional Foods and Restaurants	.9	– 36%
Total Diversified Businesses Area	\$15.9	– 21%

*Results of the Marx Toys operations sold are not included.

†Operating income is defined as income before net interest expense and income taxes.

Chemicals

Turning to the Chemicals Division, operating income for the first quarter was at the breakeven point. The reason for this very disappointing performance is two-fold. The most important is a significant decline in sales for the year to date, caused partially by a depression in the segment of the foundry industry where we do a large part of our volume, partially by increased competition, and partially by customers working off inventories they accumulated to protect themselves during the many months when product availability was a problem.

The second major negative factor at the moment is that our new chemicals plant at Bayport, Texas, is running several months behind the operating schedule we had planned. Bayport, of course, represents substantial new technology for us and, realistically, we have to accept the fact that getting a complex new system operating efficiently can always present unexpected problems. In the judgment of the division's management, the problems at Bayport are likely to be resolved in the near future.

While we cannot yet predict how soon the foundry business upturn will take place, the division is maintaining substantial inventories in order to avoid any possibility of a recurrence of product shortages. We continue to believe that this division has the potential to be one of the Company's major profit centers in the future.

Now, before asking our three Executive Vice Presidents to comment specifically on their respective areas, let me make just one more comment about first-quarter results and show you just one more chart. My comment has to do with the significance of quarterly earnings, and it is simply this: Our business cannot be properly analyzed on a short-term basis, in my opinion – which is why I think this final chart of figures is important.

Consolidated Operating Income Trends†
(Millions of Dollars)

	Twelve Months Ended September 30			
	1973	1974	1975	1976
U.S. Grocery Products	\$ 42	\$ 50	\$ 65	\$ 85
International Grocery	10	17	18	24
Toys and Crafts*	22	22	24	28
Chemicals	7	12	20	9
Institutional Foods and Restaurants	1	2	8	12
Total	\$ 82	\$103	\$135	\$158

*Results of the Marx Toys operations sold are not included.

†Operating income is defined as income before net interest expense and income taxes.

These are the operating income trends since 1973 of our five major lines of businesses. They include all the first-quarter results we have been discussing here this morning.

Operating income, which is income before deducting interest and income taxes, is not always the best guide

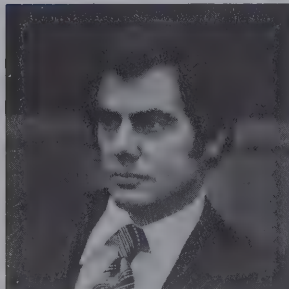
to profitability. Return on invested capital is often a better one, and there are a number of additional ways in which management performance can affect the earnings available for dividends and reinvestment in the business. However, the operating income figures on this chart do indicate, I think, that in general and over a considerable period of time, our businesses have shown good long-term earnings trends. A current exception, of course, is Chemicals, where, as I have indicated, we are cautiously optimistic about a return to the more favorable demand trends of most of the last decade.

What this chart says to me is that, by and large, Quaker's five major lines of business have shown good growth in the past, have strong positions in the marketplace today, and clearly have the potential to provide good future rewards for our shareholders and our managers alike.

Now let me introduce Bill Smithburg, Executive Vice President of our U.S. Grocery Products Area, to describe the new product activity in his area.

Mr. Smithburg

For the past year, U.S. Grocery Products has increased its efforts to develop and market new products. We have strengthened our research and development resources and intensified marketing activities behind new products.



A year ago we introduced Aunt Jemima Frozen Pancake Batter nationally. Frozen batter was a small, but rapidly growing product category, providing a good opportunity for a natural extension of our old and valued Aunt Jemima brand name. During the past year this category continued to gain by nearly half, and we took over the number-one brand position. So we have been very pleased with its progress.

This past August, we introduced Quaker Oatmeal Cookie Mix nationally. This, too, is an obvious extension of a very famous and valued old brand name. The product is an excellent value. The consumer merely adds water and, for about 89 cents, she can make three dozen delicious oatmeal cookies. Initial consumer trial has been excellent, and sales so far have exceeded expectations.

Perhaps the most significant new product is our new Ken-L Ration Tender Chunks. This is a unique product innovation in the pet food business. Primarily grain-based, it competes mostly in the largest and fastest growing dry segment of the pet food market as well as in the semi-moist category. The product is packaged in 5 lb., 10 lb., and 20 lb. bags like most dry dog foods, but is softer and more palatable than other dry products, and is less expensive than the higher priced semi-moist alternatives. It has been in six test markets since early August, and sales and initial consumer trial have been excellent.

We have two new bread mixes in test market. The first is a line of five flavors of Quick Bread Mixes. These make an excellent and tasty dinner bread that can be prepared in less than 35 minutes. It is a convenient food for those who want something better than the typical store breads for dinner, but who don't have a lot of time.

For another bread market segment we are test-marketing Quaker Homemade Bread Mix. It is made with a special imported French yeast, takes 15 to 20 minutes of preparation and about an hour and a half of baking time. The result is one of the best tasting breads you've ever tried.

We also continue to develop flavor extensions of existing successful product lines. In our pet food line, a beef-flavored canned Ken-L Ration dog food has been successfully test-marketed. A canned Puss 'n Boots cat food called Fisherman's Platter, which is a blend of tuna, salmon and shrimp, has recently been introduced nationally, following successful test marketing.

In our human foods line, a cinnamon-flavored version of our highly successful Life Cereal has just entered test market. A new cheese flavor of our growing Quaker Instant Grits line has been introduced in southern markets. Another test-market item is a mushroom flavor of our growing Celeste Pizza line.

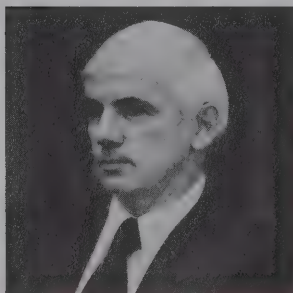
In addition to these products, which are in at least limited distribution, we have several new products currently in consumer testing. We are hopeful that our current test-market and developmental activities will lead to a continued increase in the number of new product introductions over the next few years.

Now, may I present Frank Morgan, Executive Vice President of our International Grocery Products Area.

Mr. Morgan

It is a pleasure for me to outline for you today some of the key elements of Quaker's International Grocery Products business. To put it in perspective, International Grocery Products is about half the size of the U.S. grocery business in dollar sales volume. It employs six thousand people, approximately a fourth of all Quaker employees — nearly all of whom are employed outside the United States.

Quaker has wholly owned subsidiaries in Canada, the United Kingdom, Mexico, the Benelux countries, France, Scandinavia, Brazil and Australia, in descending order of importance in terms of dollar sales. Two countries — Canada and the U.K. — account for about forty percent of the total International Grocery Products sales. Both of these companies have been an integral part of the Quaker family for a very long time. Canada is celebrating its 75th anniversary this year, and the British company is now in its 77th year. In addition to the countries where we have manufacturing facilities, there are many other countries where Quaker products are marketed. For instance, the Benelux company, headquartered in Holland, provides products to Belgium, in addition to many export markets throughout the world. Our Scandinavian company, headquartered in Denmark, sells to Sweden and Norway — and Australia services the Philippines, Malaysia and Japan. In many other areas of the world, Quaker operates with licensing, distribution, contract-manufacturing and/or joint-venture arrangements.



During the period from fiscal 1971 to fiscal 1976, sales in International Grocery Products nearly tripled. The economies of size and scale associated with this growth resulted in significantly improved profitability.

This growth resulted from increased market penetration, geographic expansion, new product development, and acquisitions. A number of products developed in the U.S. over the last ten years, such as Quaker 100% Natural Cereal and Ken-L Ration Burger dog food, are being sold internationally, in addition to our basic lines of foods and pet foods, as well as some products developed especially for specific overseas markets. Acquisitions during the past seven years accounted for more than 20 percent of our fiscal 1976 sales. They also took us into some lines of business that we are not in here in the U.S.

In Mexico, Quaker enjoys the leading share of the chocolate market, with a fine line of high-quality candy bars, table chocolate and powdered beverage products.

In Brazil, Quaker has the leading share of the canned sardine market, a very important business.

The pet food market in France is at an early stage of potentially rapid growth, and with our Fido and Fidele brands, we're in a position to take advantage of this opportunity. A product called Fido Steaky is the French counterpart of Ken-L Ration Burger here in the U.S.

Economic and political uncertainty is a significant risk in many countries. This is reflected in a number of ways, such as high inflation, price and wage controls and currency revaluations — all currently being experienced. It should be noted, however, that these are not new risks — nor is The Quaker Oats Company by any means a newcomer to the international business scene.

Our international opportunities are many. We are well-positioned to expand our fine line of Quaker products in many of the undeveloped markets of the world. As people in these countries increase their affluence and standard of living, more and more of them become potential customers for Quaker products. Geographic expansion in terms of product lines or in countries where we currently do little or no business can provide additional growth. Last, but not least, acquisitions, although more difficult in some countries than others, present still other opportunities for future growth.

Currently, the growth of International Grocery Products is increasing at a much faster rate than the U.S. Grocery Products business. We look forward with confidence to the continuation of these profitable trends.

I'd now like to introduce Arch McClure, Executive Vice President of the Diversified Businesses Area.

Mr. McClure

Although each of the Diversified Businesses has important product plans underway, I'd like to highlight the restaurant operation because there has been much stockholder interest expressed in it.



Magic Pan is growing at a faster pace than any other division in the Diversified Businesses Area, with sales increasing from \$5.6 million three years ago to \$34.7 million in fiscal 1976. The number of restaurants has increased each year, to a total of 38 last June. For this year, there is a substantial increase under way, with approval for 24 new Magic Pan locations, five of which have already been opened.

Magic Pan is in the specialty restaurant business. Crepes are featured on the menu for both entrees and desserts. The specialty restaurant business is large and growing significantly.

With the next few years' anticipated growth in the number of people in the 22 to 35-year age group, with the continuing increase in the number of career women, and with projected rises in household income, overall demographic trends appear favorable. And, importantly, the public finds eating out to be both convenient and an enjoyable experience.

To reach this growing market, the Magic Pan management concentrates on locations within easy access of their customers. The menu is distinctive and meets customer expectations for quality and variety. Pricing is moderate, and the decor objective is to provide a warm atmosphere. The final ingredient is the care of an exceptional team of restaurant managers and a friendly staff.

Performance to date has been encouraging. Restaurants have been established on a nationwide basis, and one is now open also in Toronto, Canada. New restaurant openings have been strong, and there has been continued traffic growth in the older locations.

Also, our second restaurant format, The Proud Popover, just began operations in Boston. The decor is Early American, and the menu features popovers with a variety of fillings for entrees, and cream puffs with various toppings for desserts.

Much emphasis is being placed on management training programs. Area training centers have been established at selected restaurants, where trainees take both individual and group study. Detailed courses from standard manuals and on-the-job direction by managers provide the required training for the operating staff.

The results of this training effort are seen in the attractive presentation of crepe specialties. Our enthusiastic staff is waiting to serve you on your next visit to a Magic Pan Restaurant.

Mr. Stuart

Let me mention one final dimension of our business. Earlier, I referred to several changes we had made internally that are having a very positive effect on our results. There's one other area I'd like to discuss with you that's important for the future of the company and all shareholders. That's *planning*.

Corporate Planning

We've made a number of improvements in our planning process, designed essentially to be sure we have the right combination of inputs from our research, operating, marketing and financial people—in fact, from all the relevant disciplines. This includes considerable focus on the external environments in which we operate.

To a significant degree, all members of the Board of Directors participate quite thoroughly in our strategic planning process. For the last two years, this has involved a two-day Board meeting in July focused exclusively on strategic planning – and of course, plans are also discussed and reviewed throughout the year.

You've heard me say in the past that Directors at Quaker are *working* Directors, and I want to personally thank our Board for the tremendous amount of time and energy they devote constructively to planning and every other aspect of our company. Director involvement at Quaker is at a very high and very healthy level.

Let me again refer to comments I made in the Annual Report. We had an excellent year in fiscal 1976, thanks to a number of favorable external factors as well as many internal areas in which we now run a much tighter ship. These trends generally continued through the first quarter. As Ken Mason said, we continue to see much strength in our grocery business both in the United States and worldwide. And our new product activity, both in foods and pet foods, is increasing. The toys and crafts segment is now in much better shape, after having faced last year's hard decisions regarding Marx; the Burry division is much stronger than it was just a few years ago; Magic Pan is involved in very sound growth that makes its future look bright; and the chemicals business, where we've been experiencing disappointment for close to a year, has good long-term potential. When you add to these points our new senior management organization, our increased financial strength and our expectations of progress, I think you'll agree that Quaker is in sound shape in this, the 100th year of our best-known, worldwide trademark – The Quaker Man.

All shareholders present were invited to join the discussion of each matter voted on at the Annual Meeting — the election of a new Board and all of the Directors' and Shareholder proposals. At these times as well as during the discussion period at the end of the meeting, several questions were raised — almost all of them by a single shareholder — that dealt with various aspects of conflict of interest. Included were questions about qualifications of Directors, Company controls on improper political contributions, and retainer relationships with outside legal counsel. Mr. Stuart indicated that the Board, members of senior management and legal counsel have been consistently diligent to assure that the Company's business is conducted on a sound ethical basis.

Other questions raised at the meeting include:

Why was Marx Toys sold less than four years after acquisition?

During the period of Quaker ownership, Marx experienced a number of business reversals, related to difficulties in obtaining raw materials, product design and distribution. Strategic changes did not effect improvement. The findings of a study authorized by the Board more than a year ago were that Marx no longer represented a good investment for Quaker because a better return on those investment dollars could be obtained elsewhere. Most of Marx was sold on April 15, 1976.

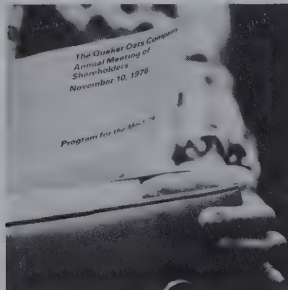
How much was contributed to charity last year?

In fiscal 1976, the Company and The Quaker Oats Foundation contributed approximately \$913,000. Almost half of this amount went to educational institutions and organizations, and a little more than a quarter of the total was in support of united giving appeals in various locations. The balance was contributed for youth programs and urban affairs, health care, arts and culture and civic projects.

Who votes the common shares in the employees' Quaker Stock Fund?

These shares are voted by the Fund's trustee at its own discretion, without prior consultation with the Company.

Other discussion. Shareholders present at the meeting also discussed other matters already covered in the 1976 Annual Report, which was mailed to all shareholders in September.



First Interim Report

Three Months Ended September 30, 1976

On November 10, 1976, the Company reported improved sales and earnings for the first quarter of the 1977 fiscal year.

Per-share earnings of \$1.14 and net income of \$25 million were each 3 percent higher than the record \$1.11 a share and \$24.3 million in the strong first quarter of a year ago, when earnings were very substantially higher than any prior first quarter in the Company's history. Prior-year numbers are shown on a pro forma basis to make them comparable with current-year changes in the valuation of certain inventories and the recording of certain advertising and merchandising expenses.

First-quarter sales were \$394.1 million, up 2 percent from last year's \$385.7 million. The prior-year period included \$20.4 million of sales from the Marx Toys operations that were sold last April. Sales in continuing businesses are 8 percent ahead of last year's first quarter.

This year's good first-quarter results reflect a modest increase in operating income in U.S. Grocery Products and a significant increase for International Grocery Products, both on good sales increases.

The Toys and Crafts category had a satisfactory quarter, with the Marx Toys losses now out of the system. Excluding Marx from last year's results, sales in this category were up 12 percent, and operating income was slightly below the prior year.

As previously reported, the Chemicals Division's furfural and furfuryl alcohol products have experienced a significant fall-off in sales due to reduced activity in the worldwide foundry industry and strong competitive pressures. In addition, our new chemicals plant at Bayport, Texas, is experiencing production delays and is now a few months behind schedule. Sales of chemicals declined 9 percent on lower volumes, and operating income was only slightly above the break-even point. Despite the difficulty in predicting the timing of a turn-around in this business, we continue to be confident in the division's long-term potential as a major contributor to earnings.

Institutional Foods and Restaurants, consisting of Magic Pan Creperies and the Burry Division, showed a 19 percent sales increase. Operating income in the quarter declined slightly, due largely to increased costs at Burry.

The Company's improved cash position resulted in a 36 percent decline in net interest expense to \$2.9 million.

Effective with this interim report, sales and operating income data will be reported in line-of-business categories each quarter instead of just at year-end in the annual report.

Complete details of the accounting changes made this year are discussed beginning on page 33.

The Quaker Oats Company and Subsidiaries
Sales and Operating Income

	Millions of Dollars	
Three Months Ended September 30	1976	1975*
U.S. Grocery Products Area	\$ 183.5	\$ 171.4
	29.4	28.7
International Grocery Products Area	87.3	79.9
	7.7	6.0
Diversified Businesses Area		
Toys and Crafts	73.6	66.0
	14.9	15.4
Chemicals	23.9	26.4
	.1	3.3
Institutional Foods and Restaurants	25.8	21.6
	.9	1.4
Total Diversified Businesses Area	123.3	114.0
	15.9	20.1
Total Continuing Businesses	394.1	365.3
	53.0	54.8
Marx operations sold	—	20.4
	—	(1.7)
Total Sales	394.1	385.7
Total Operating Income	53.0	53.1
Less interest expense—net	2.9	4.5
Income before income taxes	\$ 50.1	\$ 48.6

*Operating income, defined as income before net interest expense and income taxes, is on a pro forma basis, assuming that July 1, 1976, accounting changes in the method of pricing selected interim inventories and accounting for certain interim advertising and merchandising expenses were applied retroactively.

Sales figures—Black ink

Operating income figures—Blue ink

The Quaker Oats Company and Subsidiaries
Condensed Statement of Consolidated Income (Unaudited)

	Thousands of Dollars	
Three Months Ended September 30	1976	1975
Net Sales	\$394,083	\$385,666
Cost of goods sold	<u>268,076</u>	<u>263,742</u>
Gross profit	<u>126,007</u>	<u>121,924</u>
Selling, general and administrative expenses	75,193	72,018
Interest expense — net	2,892	4,472
Other (income) expense	<u>(2,153)</u>	<u>1,379</u>
Income Before Income Taxes	50,075	44,055
Provision for income taxes	<u>25,088</u>	<u>22,027</u>
Net Income	24,987	22,028
Preferred and preference dividends	<u>1,301</u>	<u>1,301</u>
Net Income Available for Common	<u>\$ 23,686</u>	<u>\$ 20,727</u>
Per Common Share:		
Net income	\$ 1.14	\$ 1.00
Dividends declared	\$.23	\$.21
Average Common Shares Outstanding	20,732,136	20,699,014
Pro forma amounts assuming fiscal 1977 accounting changes were applied retroactively		
Net income		<u>\$ 24,329</u>
Net income per common share		<u>\$ 1.11</u>

Notes

1. Interim results are not necessarily indicative of performance for the full year.
2. See page 33 for a complete discussion of accounting changes made in fiscal 1977.

Condensed Consolidated Balance Sheet (Unaudited)
Assets

	Thousands of Dollars	
September 30	1976	1975
Current Assets:		
Cash and marketable securities	\$ 41,655	\$ 4,981
Receivables — net	207,472	209,818
Inventories	209,085	201,108
Prepaid expenses	12,645	9,860
Current assets	470,857	425,767
Other Receivables and Investments	13,480	7,219
Property, Plant and Equipment	531,231	507,692
Less accumulated depreciation	150,899	141,441
Properties — net	380,332	366,251
Intangible Assets	42,482	47,388
	\$907,151	\$846,625

The Quaker Oats Company and Subsidiaries
Liabilities and Shareholders' Equity

	Thousands of Dollars	
September 30	1976	1975
Current Liabilities:		
Short-term debt	\$ 60,496	\$ 65,349
Accounts payable and accrued expenses	131,099	119,625
Income taxes payable	44,386	22,686
Current maturities of long-term debt	390	10,765
Dividends payable	6,070	5,648
Current liabilities	242,441	224,073
Long-Term Debt	148,411	147,887
Other Liabilities	14,216	9,489
Deferred Income Taxes	51,295	48,043
Shareholders' Equity:		
Preferred, \$50 par value, \$3 cumulative convertible, authorized 147,553 and 147,831 shares, respectively; issued 141,821 and 142,099 shares, respectively	7,091	7,105
Preference, without par value, \$100 stated value, \$9.56 cumulative, authorized 1,500,000 shares; issued 500,000 shares	50,000	50,000
Common, \$5 par value, authorized 35,000,000 shares; issued 20,985,581 and 20,948,934 shares, respectively	104,928	104,745
Additional paid-in capital	23,281	22,820
Reinvested earnings	271,115	238,090
	456,415	422,760
Less treasury common stock, at cost	5,627	5,627
Shareholders' equity	450,788	417,133
	\$907,151	\$846,625

The Quaker Oats Company and Subsidiaries
Condensed Consolidated Statement of Changes in Financial
Position (Unaudited)

	Thousands of Dollars	
Three Months Ended September 30	1976	1975
Sources of Funds:		
Operations		
Net income	\$ 24,987	\$ 22,028
Depreciation, amortization and deferred income taxes	10,246	9,966
Total from operations	35,233	31,994
Increase in accounts payable and accrued expenses	8,853	11,612
Increase in income taxes payable	11,207	15,871
Increase in short-term debt	14,256	36,821
Total funds provided	69,549	96,298
Uses of Funds:		
Increase in accounts receivable	68,288	65,467
Increase in inventories	10,879	12,405
Additions to properties	15,616	15,421
Decrease in long-term debt	257	10,396
Cash dividends	6,069	5,648
Excess of cost over net current assets of acquired businesses	—	5,621
Other—decrease (increase)—net	4,654	(6,034)
Total funds used	105,763	108,924
Net (decrease) in cash and marketable securities	\$ (36,214)	\$ (12,626)

Accounting Changes

Effective July 1, 1976, the Company made the following accounting changes:

1. Inventories that previously had been valued at projected average annual cost for reporting interim results are now valued at average quarterly cost.
2. Certain advertising and merchandising expenses that previously had been charged to interim periods in proportion to projected annual sales are now being expensed as incurred.

These changes were made to make the basis of reporting interim results more comparable with that of reporting full-year results; they have no effect on annual net income. Because inventory and advertising and merchandising costing is no longer based on projected annual totals, the Company expects its quarterly results will be easier to understand and evaluate.

The estimated pro forma effects of the above changes on fiscal 1976 quarterly earnings, assuming retroactive application, are as follows:

	Net Income		Earnings Per Share	
	As Reported	Pro Forma Amounts	As Reported	Pro Forma Amounts
First Quarter	\$22.0	\$24.3	\$1.00	\$1.11
Second Quarter	4.9*	5.1*	.18*	.18*
Third Quarter	15.9	14.3	.70	.63
Fourth Quarter	10.3	9.4	.43	.39
Fiscal Year	<u>\$53.1*</u>	<u>\$53.1*</u>	<u>\$2.31*</u>	<u>\$2.31*</u>

*After a net-of-tax provision of \$11.9 million, equivalent to 57 cents a share, to write-down Marx Toys operations sold on April 15, 1976, to their net realized value.

3. In accordance with the provisions of Financial Accounting Standards Board Statement No. 8, the Company also changed its method of translating non-U.S. currency transactions and financial statements. Under the new method, all translation gains and losses, both realized and unrealized, are recognized in income currently. Prior to the change, unrealized translation gains, net of previously recorded losses, were deferred. The cumulative unrealized translation reserve at June 30, 1976, of \$1.2 million was credited to income during the quarter ended Sept. 30, 1976. Prior year's operating results have not been restated to retroactively reflect the provisions of FASB Statement No. 8, because the effect is not material.

Corporate Staff

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Kenneth Mason

President and Chief Operating Officer

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Vice President — Corporate Purchasing

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Vice Chairman of the Board

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Vice President — Corporate Taxes

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Assistant Treasurer

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Vice President — Employee Relations

Luther C. McKinney

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Corporate Secretary

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Vice President and General Counsel

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Assistant Secretary

Louis J. Mallardi, Jr.

Assistant Secretary

Joann A. Pitcher

Assistant Secretary

Howard J. Thomas, Jr.

Assistant Secretary

M. Gail Waller

Assistant Secretary

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Area Staff

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Raymond C. Eggleston
Vice President and Controller

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Clifford F. Lynch
Vice President—Distribution

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Vice President—Advertising,
President, AdCom, Inc.

Joan G. Stark
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Vice President and Scientific Advisor

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Vice President — Engineering
Charles J. Weinschreider
Vice President — Marketing
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Vice President — Operations

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(Specialized Glass and
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Corporate Affairs

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***Member of the Executive Committee**

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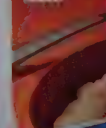


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**Interim Report
Six Months and Second Quarter**

Ended December 31, 1976



The Quaker Oats Company

To Our Shareholders:



Net income for our first fiscal half ended December 31, 1976, was \$41.1 million, or \$1.86 per common share, compared with a pro forma \$29.4 million, or \$1.29 per share for the same period a year ago. Last year's earnings included a 57 cents provision related to the sale of Marx Toys operations, which took place in April, 1976. Consolidated sales for the half were \$791.2 million, compared with \$780.5 million last year (which included Marx sales of \$38 million). Sales of continuing businesses were 7 percent ahead of last year for the six-month period.

Second-quarter net income was 72 cents a share, compared with 18 cents in the same period last year when the 57 cents provision was recorded. Second-quarter sales were \$397.1 million, 5 percent ahead of the second quarter last year on the basis of continuing businesses.

Results for the six-month and second-quarter periods were good in all lines of business except the Chemicals Division.

Operating Income

First-half operating income in U.S. Grocery Products, though slightly below last year's record level as a result of stepped-up marketing support for new and established products, was very significantly higher than any other comparable prior period in the Company's history. International Grocery Products operating income was about the same as last year, even though there was a decline in the second quarter largely due to the devaluation of the Mexican peso. During the half, the Magic Pan Restaurants Division opened twelve new locations. Thirteen more are planned for the next six months, for an expected total of 63 at fiscal year-end.

Operating income in Toys and Crafts was up, aided by a good Christmas season at Fisher-Price Toys. For the 1976 calendar year, Fisher-Price sales were \$181.3 million, up 15 percent from the prior calendar year.

Chemicals Division

Dollar sales in the Chemicals Division for the first six months were off 5 percent, and unit sales were down about 20 percent. The division posted a \$1.5 million operating loss for the half, including an \$800,000 write-off related to the closing of our small furfuryl alcohol manufacturing facility in the United Kingdom, which we announced January 19. European chemicals production is now consolidated in Belgium.

The sales weakness in chemicals has lasted longer than anticipated, principally due to strong competitive activity and continued market softness.

Several actions were taken in January to focus our Company's highest priority on improving the Chemicals Division's operating results. Organizationally, the Division now reports to Kenneth Mason, President and Chief Operating Officer, and several other changes have been made to strengthen Divisional operations and marketing organizations, and intensify marketing efforts.

The timing of the turnaround in chemicals still cannot be predicted, but we continue to believe the long-term potential of this business is good.

Montron Acquisition

We also recently completed the cash purchase of Montron Corporation, Mountain View, California, for about \$3.5 million. Montron, a specialty manufacturer of audio-visual toys, will operate under Fisher-Price management.

A handwritten signature in blue ink, reading "Robert D. Stuart, Jr." with a stylized flourish at the end.

Robert D. Stuart, Jr.
Chairman and Chief Executive Officer

February 15, 1977

The Quaker Oats Company and Subsidiaries
Sales and Operating Income[†] (Unaudited)

	Millions of Dollars			
	Three Months Ended December 31		Six Months Ended December 31	
	1976	1975	1976	1975
U.S. Grocery Products Area*	\$183.1	\$179.9	\$366.6	\$351.3
	20.0	23.7	49.4	52.4
International Grocery Products Area*	87.0	85.2	174.3	165.1
	4.2	6.0	11.9	12.0
Diversified Businesses Area				
Toys and Crafts	72.3	63.1	145.9	129.1
	10.1	8.3	25.0	23.7
Chemicals	27.1	27.5	51.0	53.9
	(1.6)	4.0	(1.5)	7.3
Institutional Foods and Restaurants	27.6	21.5	53.4	43.1
	2.0	2.3	2.9	3.7
Total Diversified Businesses Area	127.0	112.1	250.3	226.1
	10.5	14.6	26.4	34.7
Total Continuing Businesses	397.1	377.2	791.2	742.5
	34.7	44.3	87.7	99.1
Marx operations sold	—	17.6	—	38.0
	—	(29.6)**	—	(31.3)**
Total Sales	397.1	394.8	791.2	780.5
Total Operating Income	34.7	14.7	87.7*	67.8
Less interest expense—net	3.4	3.8	6.3	8.3
Income before income taxes	\$ 31.3	\$ 10.9	\$ 81.4	\$ 59.5

Sales figures—Black ink

Operating income figures—Blue ink

[†]Operating income is defined as income before net interest expense and income taxes. Amounts for the periods ending December 31, 1975, are on a pro forma basis assuming that July 1, 1976, accounting changes in the method of pricing selected interim inventories and accounting for certain interim advertising and merchandising expenses were applied retroactively.

*Results of Canadian grocery products operations are now included in the International Grocery Products Area, consistent with organizational changes made effective this fiscal year.

**After a pre-tax provision of \$24.8 million, equivalent to 57 cents a share, to write-down Marx Toys operations sold on April 15, 1976.

The Quaker Oats Company and Subsidiaries
Condensed Statement of Consolidated Income (Unaudited)

	Thousands of Dollars			
	Three Months Ended		Six Months Ended	
	December 31		December 31	
	1976	1975	1976	1975
Net Sales	\$397,116	\$394,840	\$791,199	\$780,506
Cost of goods sold	273,662	271,602	541,738	535,344
Gross profit	123,454	123,238	249,461	245,162
Selling, general and administrative expenses	89,039	81,552	164,232	153,570
Interest expense—net	3,412	3,782	6,304	8,254
Other (income) expense	(357)	27,441	(2,510)	28,820
Income Before Income Taxes	31,360	10,463	81,435	54,518
Provision for income taxes	15,222	5,525	40,310	27,552
Net Income	16,138	4,938	41,125	26,966
Preferred and preference dividends	1,302	1,302	2,603	2,603
Net Income Available for Common	\$ 14,836	\$ 3,636	\$ 38,522	\$ 24,363
Per Common Share:				
Net income	\$.72	\$.18(2)	\$ 1.86	\$ 1.18(2)
Dividends declared	\$.23	\$.21	\$.46	\$.42
Average Common Shares Outstanding	20,741,251	20,700,738	20,736,840	20,699,998

Pro forma amounts assuming fiscal 1977 accounting changes were applied retroactively:

Net income	<u>\$ 5,086</u>	<u>\$ 29,415</u>
Net income per common share	<u>\$.18(2)</u>	<u>\$ 1.29(2)</u>

Notes

- Interim results are not necessarily indicative of performance for the full year.
- After a write-down to estimated realizable value, less selling costs, of the Marx Toys operations in the U.S., Canada and Hong Kong, which were sold in April, 1976, as a going concern, equivalent to 57 cents a share.
- See page 8 for a complete discussion of accounting changes made in fiscal 1977.

The Quaker Oats Company and Subsidiaries
Condensed Consolidated Statement of Changes in Financial Position
(Unaudited)

Thousands of Dollars

Six Months Ended December 31

	1976	1975
Sources of Funds:		
Operations		
Net income	\$ 41,125	\$ 26,966
Depreciation, amortization and deferred income taxes	21,512	17,056
Provision for loss on sale of Marx non-current assets	—	9,100
Total from operations	<u>62,637</u>	<u>53,122</u>
Sale of properties	3,204	1,862
Increase in short-term debt	5,063	24,740
Increase in accounts payable and accrued expenses	4,135	14,475
Total funds provided	<u>75,039</u>	<u>94,199</u>
Uses of Funds:		
Increase (decrease) in receivables — net	7,446	(7,638)
Increase in inventories	13,759	1,591
Additions to properties	33,111	32,051
Excess of cost over net current assets of acquired businesses	—	5,557
Decrease (increase) in income taxes payable	6,346	(11,100)
Decrease in long-term debt	784	20,790
Cash dividends	12,142	11,298
Other — decrease — net	3,499	483
	<u>77,087</u>	<u>53,032</u>
Net increase (decrease) in cash and marketable securities	<u>\$ (2,048)</u>	<u>\$ 41,167</u>

Condensed Consolidated Balance Sheet (Unaudited)
Assets

	Thousands of Dollars	
December 31	1976	1975
Current Assets:		
Cash and marketable securities	\$ 75,821	\$ 58,774
Receivables—net	146,630	136,713
Inventories	211,965	190,294
Prepaid expenses	10,759	9,294
Current assets	445,175	395,075
Other Receivables and Investments	13,580	6,686
Property, Plant and Equipment	540,241	521,314
Less accumulated depreciation	153,965	155,261
Properties—net	386,276	366,053
Intangible Assets	42,067	44,682
	<u>\$887,098</u>	<u>\$812,496</u>

The Quaker Oats Company and Subsidiaries

Liabilities and Shareholders' Equity

	Thousands of Dollars	
December 31	1976	1975
Current Liabilities:		
Short-term debt	\$ 51,303	\$ 53,268
Accounts payable and accrued expenses	126,381	122,488
Income taxes payable	26,833	17,915
Current maturities of long-term debt	243	572
Dividends payable	6,071	5,650
Current liabilities	<u>210,831</u>	<u>199,893</u>
Long-Term Debt	147,884	137,493
Other Liabilities	14,207	12,525
Deferred Income Taxes	53,054	46,068
Shareholders' Equity:		
Preferred, \$50 par value, \$3 cumulative convertible, authorized 147,553 and 147,811 shares, respectively; issued 141,821 and 142,079 shares, respectively	7,091	7,104
Preference, without par value, \$100 stated value, \$9.56 cumulative, authorized 1,500,000 shares; issued 500,000 shares	50,000	50,000
Common, \$5 par value, authorized 35,000,000 shares; issued 20,995,962 and 20,955,758 shares, respectively	104,979	104,779
Additional paid-in capital	23,431	22,883
Reinvested earnings	281,180	237,378
	<u>466,681</u>	<u>422,144</u>
Less treasury common stock, at cost	5,559	5,627
Shareholders' equity	<u>461,122</u>	<u>416,517</u>
	<u>\$887,098</u>	<u>\$812,496</u>

Accounting Changes

As stated in the first interim report, effective July 1, 1976, the Company made the following accounting changes:

1. Inventories that previously had been valued at projected average annual cost for reporting interim results are now valued at average quarterly cost.
2. Certain advertising and merchandising expenses that previously had been charged to interim periods in proportion to projected annual sales are now being expensed as incurred.

These changes were made to make the basis of reporting interim results more comparable with that of reporting full-year results; they have no effect on annual net income. Because inventory and advertising and merchandising costing is no longer based on projected annual totals, the Company expects its quarterly results will be easier to understand and evaluate.

3. In accordance with the provisions of Financial Accounting Standards Board Statement No. 8, the Company also changed its method of translating non-U.S. currency transactions and financial statements. Under the new method, all translation gains and losses, both realized and unrealized, are recognized in income currently. Prior to the change, unrealized translation gains, net of previously recorded losses, were deferred. The cumulative unrealized translation reserve at June 30, 1976, of \$1.2 million was credited to income during the quarter ended Sept. 30, 1976. Prior year's operating results have not been restated to retroactively reflect the provisions of FASB Statement No. 8 because the effect is not material.

Assuming that the changes in the way we value inventories and record certain advertising and merchandising expenses on an interim basis were applied retroactively, fiscal 1976 quarterly operating income and earnings (unaudited) would be as shown on the opposite page:

	Millions of Dollars Except Per Share				
	First Quarter (Sept. 30)	Second Quarter (Dec. 31)	Third Quarter (Mar. 31)	Fourth Quarter (June 30)	Full Fiscal Year
U.S. Grocery Products Area*	\$28.7	\$23.7	\$22.4	\$ 9.4	\$84.2
International Grocery Products Area*	6.0	6.0	6.3	4.1	22.4
Diversified Businesses Area					
Toys and Crafts	15.4	8.3	(.9)	6.2	29.0
Chemicals	3.3	4.0	5.4	(.9)	11.8
Institutional Foods and Restaurants	<u>1.4</u>	<u>2.3</u>	<u>5.8</u>	<u>2.8</u>	<u>12.3</u>
Total Diversified Businesses Area	<u>20.1</u>	<u>14.6</u>	<u>10.3</u>	<u>8.1</u>	<u>53.1</u>
Total Continuing Businesses	54.8	44.3	39.0	21.6	159.7
Marx operations sold	<u>(1.7)</u>	<u>(29.6)</u>	<u>(4.1)</u>	<u>—</u>	<u>(35.4)</u>
Total Operating Income	53.1	14.7	34.9	21.6	124.3
Interest expense — net	<u>4.5</u>	<u>3.8</u>	<u>2.7</u>	<u>2.4</u>	<u>13.4</u>
Income Before Income Taxes	48.6	10.9	32.2	19.2	110.9
Income taxes	<u>24.3</u>	<u>5.8</u>	<u>17.9</u>	<u>9.8</u>	<u>57.8</u>
Net Income	<u>\$24.3</u>	<u>\$ 5.1</u>	<u>\$14.3</u>	<u>9.4</u>	<u>\$53.1</u>
Net Income Per Share	<u>\$1.11</u>	<u>\$.18⁽¹⁾</u>	<u>\$.63</u>	<u>\$.39</u>	<u>\$2.31⁽¹⁾</u>
As Originally Reported:					
Net Income	<u>\$22.0</u>	<u>\$ 4.9</u>	<u>\$15.9</u>	<u>\$10.3</u>	<u>\$53.1</u>
Net Income Per Share	<u>\$1.00</u>	<u>\$.18⁽¹⁾</u>	<u>\$.70</u>	<u>\$.43</u>	<u>\$2.31⁽¹⁾</u>

*Results of Canadian grocery products operations are now included in the International Grocery Products Area, consistent with organizational changes made effective this fiscal year.

(1) After a provision, equivalent to 57 cents a share, to write-down Marx Toys operations sold on April 15, 1976.

The Quaker Oats Company

Merchandise Mart Plaza Chicago, Illinois 60654



NEWS RELEASE

The Quaker Oats Company, Merchandise Mart Plaza, Chicago, Illinois 60654

Aug 25, 1976

Further Information

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NEW RECORDS FOR
QUAKER OATS YEAR-END
SALES AND EARNINGS

FOR IMMEDIATE RELEASE

Chicago, Aug. 25, 1976 -- Record sales and earnings were reported by The Quaker Oats Company today for the 1976 fiscal year ended June 30.

Per-share earnings of \$2.31 were after a 57 cents write-off taken at mid-year in connection with the April 15 sale of Marx Toys operations. After the write-off, the per-share earnings were 59 percent ahead of \$1.45 reported last year, and 13 percent better than the \$2.04 earned in fiscal 1973, Quaker's prior record year, according to Robert D. Stuart, Jr., President and Chief Executive Officer.

(MORE)

Record Quaker Sales and Earnings -- Add One

Consolidated sales were \$1.473 billion, a 6 percent increase over last year's \$1.389 billion.

Improvements in U.S. and international grocery products led the fine results, with operating earnings of \$106.6 million, 72 percent ahead of the prior year, Mr. Stuart said. Sales and operating earnings of four of Quaker's diversified businesses -- the Fisher-Price Toys, Magic Pan Restaurants, Burry and Needlecraft Divisions -- were up significantly, with operating income of \$41.3 million, 80 percent ahead of the prior year. Of Quaker's major businesses, only the Chemicals Division was off, with operating income of \$11.8 million, down 47 percent from the prior year.

Accompanying the improved earnings, Mr. Stuart said, were a much stronger balance sheet and improved financial ratios. Operating income margins -- except for Chemicals -- were significantly improved, he said, and return on common shareholders' equity was 12.8 percent, compared with 8.7 percent a year ago. Corporate financial objectives for the year were exceeded, he said.

(MORE)

THE QUAKER OATS COMPANY AND SUBSIDIARIES
SALES AND OPERATING INCOME BY AREA

Millions of Dollars

Year Ended June 30	<u>1976</u>	<u>1975</u>
SALES		
U.S. and Canadian Grocery Products	\$ 759.8	\$ 735.0
International Grocery Products	<u>256.6</u>	<u>224.6</u>
Total Grocery Products Area	<u>1,016.4</u>	<u>959.6</u>
Toys and Crafts	247.5	243.5
Chemicals	104.3	97.2
Institutional Foods & Restaurants	<u>104.8</u>	<u>88.7</u>
Total Diversified Businesses Area	<u>456.6</u>	<u>429.4</u>
Total Sales	<u>\$1,473.0</u>	<u>\$1,389.0</u>
OPERATING INCOME		
U.S. and Canadian	\$ 88.9	\$ 50.3
International	<u>17.7</u>	<u>11.5</u>
Total Grocery Products Area	<u>106.6</u>	<u>61.8</u>
Toys and Crafts	(6.4) (A)	3.5 (B)
Chemicals	11.8	22.1
Institutional Foods & Restaurants	<u>12.3</u>	<u>6.3</u>
Total Diversified Businesses Area	<u>17.7</u>	<u>31.9</u>
Total Operating Income	\$ 124.3	\$ 93.7
Less interest expense-net	<u>13.4</u>	<u>26.4</u>
Income before income taxes	110.9	67.3
Provision for income taxes	<u>57.8</u>	<u>36.3</u>
Net Income	<u>\$ 53.1</u>	<u>\$ 31.0</u>

(A) After a \$23.2 million pre-tax write-off provision resulting from the April, 1976 sale of the U.S., Canadian and Hong Kong operations of the Marx Toys Division (equivalent to \$.57 per share).

(B) After pre-tax toy division charges of \$6.0 million related to the elimination of certain toy lines and the consolidation of facilities (equivalent to \$.19 per share).

THE QUAKER OATS COMPANY AND SUBSIDIARIES
CONDENSED STATEMENT OF CONSOLIDATED INCOME

	Year Ended June 30		Three Months Ended June 30	
	<u>1976</u>	<u>1975</u>	<u>1976</u>	<u>1975</u>
Sales	<u>\$1,473,052,000</u>	<u>\$1,389,013,000</u>	<u>\$336,294,000</u>	<u>\$343,906,000</u>
Income before taxes	110,886,000	67,293,000	20,975,000	22,389,000
Provision for income taxes	<u>57,793,000</u>	<u>36,256,000</u>	<u>10,728,000</u>	<u>13,199,000</u>
Net income	53,093,000	31,037,000	10,247,000	9,190,000
Preferred and preference dividends	<u>5,206,000</u>	<u>1,103,000</u>	<u>1,301,000</u>	<u>783,000</u>
Net income available for common	<u>\$47,887,000</u>	<u>\$29,934,000</u>	<u>\$8,946,000</u>	<u>\$8,407,000</u>
Net income per common share	<u>\$2.31 (A)</u>	<u>\$1.45 (B)</u>	<u>\$.43</u>	<u>\$.41</u>
Average number of common shares outstanding	20,711,092	20,699,008	20,727,590	20,699,008

(A) Results are after a \$11.9 million (after-tax) write-off provision relating to the decision to sell the operations of the Marx Toys Division in the U.S., Canada and Hong Kong. The sale was completed on April 15, 1976 (equivalent to \$.57 per share).

(B) After toy division charges of \$4.0 million (after-tax) related to the elimination of certain toy lines and the consolidation of facilities (equivalent to \$.19 per share).

SUMMARY OF QUARTERLY RESULTS

	Sales		Net Income		Net Income Per Common Share	
	<u>1976</u>	<u>1975</u>	<u>1976</u>	<u>1975</u>	<u>1976</u>	<u>1975</u>
First Quarter	\$ 385,666,000	\$ 344,036,000	\$22,028,000	\$ 8,558,000	\$1.00	\$.41
Second Quarter	394,840,000	372,734,000	4,938,000	5,433,000	.18	.26
Third Quarter	356,252,000	328,337,000	15,880,000	7,856,000	.70	.37
Fourth Quarter	<u>336,294,000</u>	<u>343,906,000</u>	<u>10,247,000</u>	<u>9,190,000</u>	<u>.43</u>	<u>.41</u>
Total	<u>\$1,473,052,000</u>	<u>\$1,389,013,000</u>	<u>\$53,093,000</u>	<u>\$31,037,000</u>	<u>\$2.31</u>	<u>\$1.45</u>

